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Print Edition January 14th 2006

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The economy that Alan Greenspan will hand over when he retires as Fed chairman on January 31st is in a much less healthy state than is popularly assumed: leader

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Politics this week

Jan 12th 2006
From The Economist print edition

AP

After two years of negotiations with three European countries (Britain, France and Germany), **Iran** resumed nuclear "research" activity at its Natanz uranium-enrichment plant, prompting fresh calls from the United States, Britain, France and Germany to refer the case to the UN Security Council with a view to imposing sanctions on Iran. See article

Doctors sought to bring Ariel Sharon, **Israel's** prime minister who suffered a massive stroke last week, out of a coma; he was just able to move his left arm and his condition remained critical. Opinion polls suggested that his new party, Kadima ("Forward"), may still do well in the election due on March 28th. It looked possible that Kadima's stand-in leader, Ehud Olmert, might keep up its momentum. See article

Syria's beleaguered president, Bashar Assad, visited Saudi Arabia and Egypt in an effort to shore up support for his regime. He has refused a request to be interviewed by the United Nations commission investigating the murder last year in Lebanon of a former Lebanese prime minister, Rafik Hariri, after he had quarrelled with the Syrian leader.

International aid agencies launched an appeal for food for northern **Kenya,** where about 2.5m people risk starvation because of a drought that is also ravaging parts of Ethiopia, Somalia and Tanzania.

Hundreds of Muslim pilgrims were crushed to death on the last day of the *haj* at **Mecca**. Authorities had instituted extra precautions this year to try and avoid such accidents at the event, which attracts some 2m people. Last week, 76 pilgrims were killed when a hotel collapsed.

Is Sam the man?

The United States' Senate held confirmation hearings for **Samuel Alito**, George Bush's nominee to the Supreme Court. Judge Alito was asked about his thoughts on a range of subjects, including abortion, electoral law and the limits of presidential power. See article

Republicans in the House of Representatives began the process of choosing a new majority leader after **Tom DeLay** said he would not seek to regain the position. Mr DeLay "temporarily" stepped down from the post last September after corruption charges were brought against him in Texas. See article

New Jersey's legislature voted to suspend executions until a task-force reports later this year on the fairness of the state's death row. It is the first time a state legislature has voted to suspend the death penalty, although the last execution to take place in New Jersey occurred in 1963.

Dick Cheney was briefly hospitalised after complaining of a shortness of breath. The 64-year-old vice-president has a history of heart problems, but the White House said he was suffering from the side effects of medicine taken to treat a foot ailment this time.

Death on the wing

AP

Turkey was gripped by panic about bird flu, as human cases spread across the country. But by mid-week, just two deaths attributable to the new strain had been confirmed, and the government insisted that the disease was under control. Not all of

Turkey's neighbours were convinced: several were trying vainly to stop the disease spreading further. See article

Austria marked the start of its **European Union presidency** by inviting the European Commission to Vienna. The Austrian chancellor talked of reviving the EU constitution; Germany's Angela Merkel expressed interest, and even France's Jacques Chirac said it would be good to implement parts of the document. But the Dutch, who also voted no last summer, insisted that the constitution was dead.

Ukraine's parliament passed a motion of no confidence in the government after last week's gas-price deal with Russia. But since an election was due by the end of March in any case, the decision will have little impact. See article

Spanish police arrested 20 people suspected of recruiting Islamist militants to join the insurgency in Iraq. This is the third batch of arrests, which have pulled in a total of 46 suspects so far.

Eight people were stabbed by a man in **Moscow's** main synagogue. Russia has recently seen a rise in anti-Semitic and anti-immigrant attacks.

Liberals besieged

After the final campaign debates, the opposition Conservatives appeared to be cruising towards a victory in **Canada's** general election on January 23rd. But it was not clear whether they would win a majority of seats in the House of Commons.

Mexico and nine other Latin American countries agreed to work together to defend their emigrants in the United States, following the recent approval of a bill in the House of Representatives that would make illegal immigration a felony and order the erection of 1,125 kilometres (700 miles) of fencing along the border. See article

Peru's electoral authority disqualified Alberto Fujimori, the country's president from 1990-2000, from standing in an election in April. Mr Fujimori is in detention in Chile, pending a decision on his extradition to Peru to face corruption and human-rights charges.

Haiti's electoral authorities rescheduled a much-postponed presidential election for February 7th. Meanwhile, the Brazilian general in charge of the 9,000-strong UN peacekeeping force in Haiti was found dead in a hotel room. Officials said he appeared to have committed suicide.

Not Kyoto

Representatives of America, China, India, Japan, South Korea and Australia met in Sydney to launch a new forum aimed at promoting economic growth coupled with lower **carbon emissions**. See article

Australia announced the deployment of an additional 110 troops to **Afghanistan**. Meanwhile, NATO's secretary-general, Jaap de Hoop Scheffer, urged the Dutch parliament to speed up plans to send 1,400 troops to southern Afghanistan, where they are scheduled to join a peacekeeping expansion into former Taliban strongholds. The deployment has stoked political controversy in the Netherlands.

Seven Pakistani troops and 14 suspected militants died in fighting on **Pakistan's** Afghan border. An attack by insurgents in Baluchistan killed three soldiers and 12 militants.

Thousands of demonstrators protested in the **Mongolian** capital, Ulan Bator, after the Mongolian People's Revolutionary Party, which ruled the country for much of the 20th century, withdrew its support from the governing coalition.

More than 10m girls may have been lost to abortion and sex selection over the past 20 years in **India**, according to research published in The *Lancet*, a British medical journal.

AP

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Business this week

Jan 12th 2006
From The Economist print edition

Apple Computer's share price continued its upward spiral (having more than doubled in 2005) after Steve Jobs, the company's chief executive, reported that 14m iPod digital music players had been sold in the last quarter of 2005, three times as many as the same period in 2004, and unveiled the first Apple computers to run on Intel chips, workhorse of the PC market. See article

AOL said it had bought **Truveo**, a company that specialises in online video searches that have been available for just four months. AOL will blend Truveo's technology with its own to help users search more easily for video. The news follows last week's launch by **Google** of its new video service. See article

Germany's media regulator rejected a takeover offer by **Axel Springer**, the country's largest newspaper publisher, for **ProSiebenSat.1**, a broadcaster that controls around 45% of the German TV-advertising market. The ruling said that the merged business would have a “dominant power of opinion”. Germany's competition regulator is expected to reveal its own decision soon.

A protracted takeover battle for **Guidant** continues. After submitting a revised lower offer for the medical-device maker last year, **Johnson & Johnson** reversed course and raised its bid to $23.2 billion, which Guidant immediately recommended to shareholders. However, **Boston Scientific** made clear it would “vigorously pursue” its $25 billion offer.

GTECH, the world's biggest provider of lottery systems, agreed to a $4.8 billion takeover deal from **Lottomatica**, an Italian lottery operator that is controlled by the De Agostini publishing business.

A friend indeed

General Motors received some advice from a big investor on how to avoid bankruptcy. Jerome York, an adviser to Kirk Kerkorian who owns 7.8% of GM's shares, outlined a plan that includes cutting the annual dividend to shareholders in half; reducing the pay and perks of senior executives; and possibly spinning off brands such as Hummer and Saab. Speaking at the Detroit motor show, Mr York said the beleaguered carmaker needed to do more than rely on sacrifices from unions to turn things around.

The Bank of Italy rejected a takeover bid by **Unipol**, an insurer, for **Banca Nazionale del Lavoro.** The offer had been in doubt after Unipol's former boss became embroiled in a scandal centred on Antonio Fazio's involvement in a takeover bid for a separate Italian bank. Mr Fazio resigned as the central bank's governor last month. Analysts mooted the possibility of Banca Bilbao Vizcaya Argentaria, a Spanish bank, reviving its failed bid for BNL.

Six women at **Dresdner Kleinwort Wasserstein** filed a class-action sex-discrimination lawsuit for $1.4 billion against the investment firm at a federal court in Manhattan. The case against DKW, part of Germany's Dresdner Bank, is the latest in a long line of sex-discrimination suits brought against Wall Street firms.

Slimmer figures

Atkins Nutritionals emerged from five months in bankruptcy and produced a business strategy that drastically reduces its range of diet and health-food products. At its peak, the Atkins Diet was followed by 9% of Americans but is now observed by only 2.2%. The firm lost $341m in 2004.

P&O confirmed investor speculation that it had been approached by **PSA**, a Singaporean port operator that is owned by Temasek Holdings, the Singapore government's investment company, for a possible £3.5 billion ($6.2 billion) takeover bid. The British ports and ferries company delayed a meeting, scheduled for January 20th, that

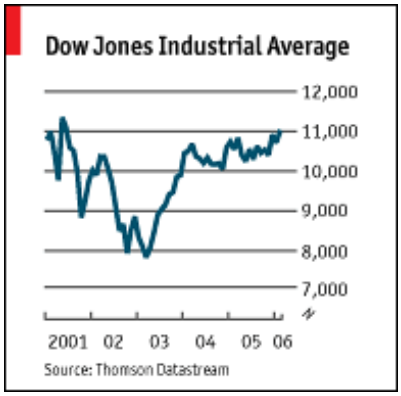
was to approve an earlier offer from Dubai's **DP World** for £3.3 billion. See article

China National Offshore Oil Corporation announced its biggest-ever overseas acquisition by agreeing to take a 45% stake in an oil and gas field in the Nigerian delta for $2.3 billion. India's Oil & Natural Gas Corporation last month won the bid to operate in the Akpo field, but the deal was rejected by the Indian government despite fierce competition with the Chinese over new energy sources.

China reported that its overall **trade surplus** stood at $102 billion in 2005, up from $32 billion in 2004. China's surplus with America was $114.7 billion, news that caused further political consternation in the United States.

Raise a glass, but sip gently

The **Dow Jones Industrial Average** stockmarket index closed above 11,000 on January 9th for the first time since June 2001. Although analysts cheered the breaching of the barrier and its positive impact on investor confidence, few expect a return to the tech-heavy boom of the late 1990s. See article



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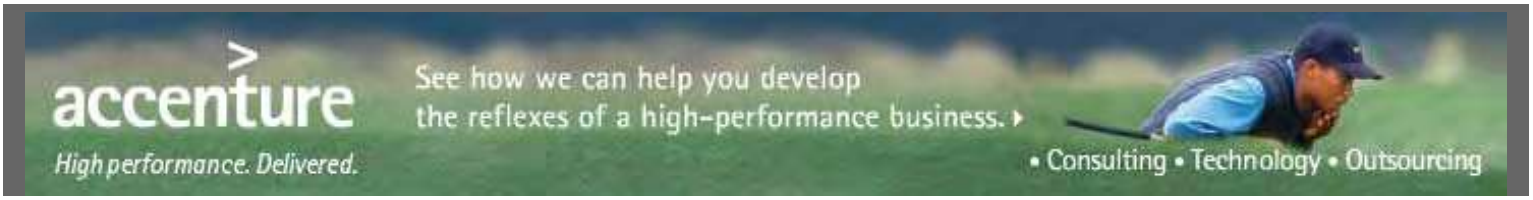
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America's economy

Danger time for America

Jan 12th 2006
From The Economist print edition

The economy that Alan Greenspan is about to hand over is in a much less healthy state than is popularly assumed

DESPITE his rather appealing personal humility, the tributes lavished upon Alan Greenspan, the chairman of the Federal Reserve, become more exuberant by the day. Ahead of his retirement on January 31st, he has been widely and extravagantly acclaimed by economic commentators, politicians and investors. After all, during much of his 18½ years in office America enjoyed rapid growth with low inflation, and he successfully steered the economy around a series of financial hazards. In his final days of glory, it may therefore seem churlish to question his record. However, Mr Greenspan's departure could well mark a high point for America's economy, with a period of sluggish growth ahead. This is not so much because he is leaving, but because of what he is leaving behind: the biggest economic imbalances in American history.

One should not exaggerate Mr Greenspan's influence—both good and bad—over the economy. Like all central bankers he is constrained by huge uncertainties about how the economy works, and by the limits of what monetary policy can do (it can affect inflation, but it cannot increase the long-term rate of growth). He controls only short-term interest rates, not bond yields, taxes or regulation. Yet for all these constraints, Mr Greenspan has long been the world's most important economic policy maker—and during an exceptional period when globalisation and information technology have been transforming the world economy. His reign has coincided with the opening up to trade and global capital flows of China, India, the former Soviet Union and many other previously closed economies. And Mr Greenspan's policies have helped to support globalisation: the robust American demand and huge appetite for imports that he facilitated made it easier for these economies to emerge and embrace open markets. The benefits to poorer nations have been huge.

So far as the American economy is concerned, however, the Fed's policies of the past decade look like having painful long-term costs. It is true that the economy has shown amazing resilience in the face of the bursting in 2000-01 of the biggest stockmarket bubble in history, of terrorist attacks and of a tripling of oil prices. Mr Greenspan's admirers attribute this to the Fed's enhanced credibility under his charge. Others point to flexible wages and prices, rapid immigration, a sounder banking system and globalisation as factors that have made the economy more resilient to shocks.

The economy's greater flexibility may indeed provide a shock-absorber. A spurt in productivity has also boosted growth. But the main reason why America's growth has remained strong in recent years has been a massive monetary stimulus. The Fed held real interest rates negative for several years, and even today real rates remain

low. Thanks to globalisation, new technology and that vaunted flexibility, which have all helped to reduce the prices of many goods, cheap money has not spilled into traditional inflation, but into rising asset prices instead—first equities and now housing. *The Economist* has long criticised Mr Greenspan for not trying to restrain the stockmarket bubble in the late 1990s, and then, after it burst, for inflating a housing bubble by holding interest rates low for so long (see article). The problem is not the rising asset prices themselves but rather their effect on the economy. By borrowing against capital gains on their homes, households have been able to consume more than they earn. Robust consumer spending has boosted GDP growth, but at the cost of a negative personal saving rate, a growing burden of household debt and a huge current-account deficit.

Burning the furniture

Ben Bernanke, Mr Greenspan's successor, likes to explain America's current-account deficit as the inevitable consequence of a saving glut in the rest of the world. Yet a large part of the blame lies with the Fed's own policies, which have allowed growth in domestic demand to outstrip supply for no less than ten years on the trot. Part of America's current prosperity is based not on genuine gains in income, nor on high productivity growth, but on borrowing from the future. The words of Ludwig von Mises, an Austrian economist of the early 20th century, nicely sum up the illusion: “It may sometimes be expedient for a man to heat the stove with his furniture. But he should not delude himself by believing that he has discovered a wonderful new method of heating his premises.”

As a result of weaker job creation than usual and sluggish real wage growth, American incomes have increased much more slowly than in previous recoveries. According to Morgan Stanley, over the past four years total private-sector labour compensation has risen by only 12% in real terms, compared with an average gain of 20% over the comparable period of the previous five expansions. Without strong gains in incomes, the growth in consumer spending has to a large extent been based on increases in house prices and credit. In recent months Mr Greenspan himself has given warnings that house prices may fall, and that this in turn could cause consumer spending to slow. In addition, he suggests that foreigners will eventually become less eager to finance the current-account deficit. Central banks in Asia and oil-producing countries have so far been happy to buy dollar assets in order to hold down their own currencies. However, there is a limit to their willingness to keep accumulating dollar reserves. Chinese officials last week offered hints that they are looking eventually to diversify China's foreign-exchange reserves. Over the next couple of years the dollar is likely to fall and bond yields rise as investors demand higher compensation for risk.

When house-price rises flatten off, and therefore the room for further equity withdrawal dries up, consumer spending will stumble. Given that consumer spending and residential construction have accounted for 90% of GDP growth in recent years, it is hard to see how this can occur without a sharp slowdown in the economy.

Handovers to a new Fed chairman are always tricky moments. They have often been followed by some sort of financial turmoil, such as the 1987 stockmarket crash, only two months after Mr Greenspan took over. This handover takes place with the economy in an unusually vulnerable state, thanks to its imbalances. The interest rates that Mr Bernanke will inherit will be close to neutral, neither restraining nor stimulating the economy. But America's domestic demand needs to grow more slowly in order to bring the saving rate and the current-account deficit back to sustainable levels. If demand fails to slow, he will need to push rates higher. This will be risky, given households' heavy debts. After 13 increases in interest rates, the tide of easy money is now flowing out, and many American households are going to be shockingly exposed. In the words of Warren Buffett, “It's only when the tide goes out that you can see who's swimming naked.”

How should Mr Bernanke respond to falling house prices and a sharp economic slowdown when they come? While he is even more opposed than Mr Greenspan to the idea of restraining asset-price bubbles, he seems just as keen to slash interest rates when bubbles burst to prevent a downturn. He is likely to continue the current asymmetric policy of never raising interest rates to curb rising asset prices, but always cutting rates after prices fall. This is dangerous as it encourages excessive risk taking and allows the imbalances to grow ever larger, making the eventual correction even worse. If the imbalances are to unwind, America needs to accept a period in which domestic demand grows more slowly than output.

The big question is whether the rest of the world will slow too. The good news is that growth is becoming more broadly based, as demand in the euro area and Japan has been picking up, and fears about an imminent hard landing in China have faded. America kept the world going during troubled times. But now it is time for others to take the lead.

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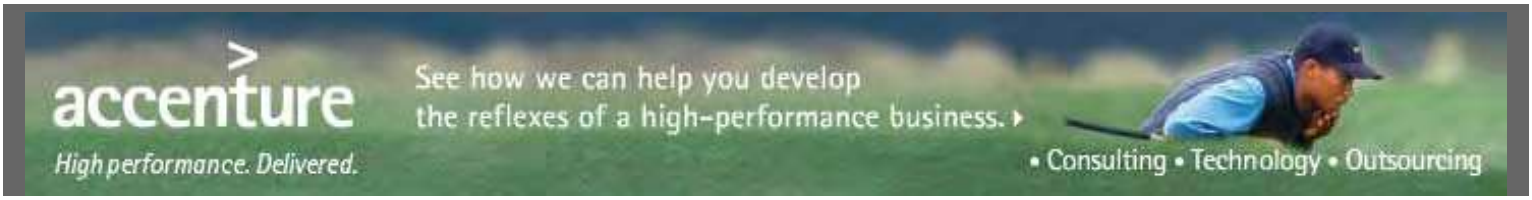
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Nuclear proliferation

Misreading Iran

Jan 12th 2006
From The Economist print edition

It wants more than reassurance

AP

ESPECIALLY since the election last June of its fire-breathing president, Mahmoud Ahmadinejad, he who denies the Holocaust and calls for the removal of Israel, Iran is often portrayed as dangerous, irrational and unpredictable. In truth, it is not irrational. It has so far played a shrewd and winning hand both in Iraq and in its nuclear game of cat-and-mouse with America, Europe and the International Atomic Energy Agency. Nor is it unpredictable. Although the timing may have surprised, Iran's crossing this week of yet another “red line” by resuming work—research only, you understand—at its uranium-enrichment facility in Natanz was the expected next step in a long-standing plan to put itself within a screwdriver's turn of building an atomic bomb (see article). Iran is, however, dangerous. But how dangerous? And to whom?

The grand bargain, and other possible delusions

The country with most to lose from a nuclear Iran is Israel, whose undeclared arsenal has for the past 40 years or so given it a monopoly on Armageddon in the Middle East. In 2001, Akbar Hashemi Rafsanjani, one of Iran's supposed moderates, mused that a single nuclear weapon could obliterate Israel, whereas Israel could “only damage” the world of Islam. Even so, a nuclear-armed Iran would indeed have to be irrational to strike Israel with such weapons. Barring tragic miscalculation, the main threat a nuclear-armed Iran would pose is not the direct use of those weapons but two second-order dangers. One is that an Iran with a nuclear deterrent might feel emboldened to pursue a more adventurous foreign policy. The other danger, related to the first, is that if Iran were to go nuclear many other countries in this uniquely combustible region—Saudi Arabia, Egypt, Syria and Turkey, to name just four—will be sorely tempted to follow.

It is often said in defence of Iran's nuclear appetite that this is a country with good reason to want a way to deter its enemies. Israel has never attacked it, and would have no conceivable reason to do so if the Iranians left it in peace. But Iran does have recent experience of invasion. The eight-year war Saddam Hussein forced on it in the 1980s cost perhaps a million Iranian lives. Today the armed forces of a hostile America are encamped in neighbouring Iraq and Afghanistan. Iranians listen to the talk of regime change from Washington, and remember how British and American spies helped to fell a nationalist Iranian government in 1953. Given both its recent history and present predicament, Iran's fears are understandable, says one appealing school of thought in the West. The best way to wean it from its nuclear obsession is therefore to offer it security and reassurance—a “grand bargain”, perhaps, that would end its quarter-century estrangement from the United States.

Maybe. However, there is a less soothing possibility. With Iraq under American occupation, and the occupiers in trouble, Iran no longer faces a threat (except, perhaps, in the realm of ideology) from its historical foe. If Iran wants a “grand bargain”, why did it snub the efforts of Britain, France and Germany to broker one, even after they had won the tacit support of George Bush? Applying Occam's razor, the simplest answer may be that Iran just isn't the status quo power the soothers want to think it is. Its leaders, if not its people, remain loyal to Khomeini's legacy —intent both on mastering their region and fulfilling Iran's destiny as the vanguard of militant Islam.

If that is the case, it is not only Israel that has much to fear if Iran breaks out of the Nuclear Non-Proliferation Treaty to go nuclear. So does America, which in Iran may come to face an even more potent opponent than al-Qaeda to Mr Bush's vision of spreading secular democracy in the Middle East. So do the Arab regimes whose fear of Iran prompted them to bankroll Saddam Hussein's war against Ayatollah Khomeini, and which in some cases will react to a nuclear Iran by making or buying nuclear weapons of their own. A nuclear-armed Middle East on its doorstep can hardly be in Russia's interest either.

Which theory of Iran is right? The regime is opaque. Maybe there are two Irans, oscillating at different times between fear and ambition. Whichever is the case, it is clear by now that relying on talk alone to stop Iran from going nuclear has failed. It is time to go to the UN Security Council and try sanctions.

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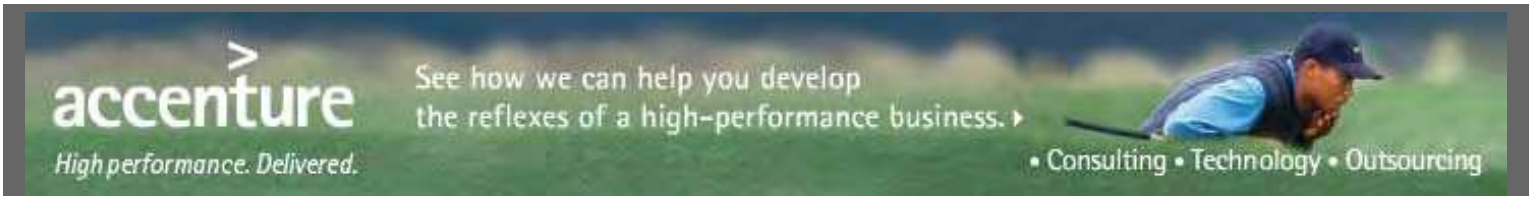
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UN reform

Fix it or scrap it

Jan 12th 2006
From The Economist print edition

Serial violators of human rights should be booted off the human-rights commission

THE United Nations was founded to promote peace, prosperity and human rights. It is doing somewhat better on the first two counts than its critics sometimes make out. The last, however, has been such a failure that it is threatening to bring the whole edifice down. Once revered as the creator of all the great universal human-rights rules and instruments, the 53-member Commission on Human Rights has been thoroughly discredited. If it cannot be fixed it needs to be scrapped. In its present form it serves only to make a mockery of the cause.

The reason for this is simple enough. The present committee is packed with members who are themselves serial abusers of human rights. Kofi Annan, the UN secretary-general, admits that their main purpose in being on the committee is not to strengthen human rights but to protect themselves from criticism. At present, these members include exemplars of virtue such as Zimbabwe, Sudan, China, Cuba, Saudi Arabia, Nepal and Russia—a veritable roll call of the worst offenders.

A plan of sorts exists to reform this mess. Mr Annan called last spring for the replacement of the commission, which at present meets for just six weeks once a year, by a leaner, tougher, year-round Human Rights Council, which would be ready to act whenever serious abuse was discovered, and whose members should have a solid record on human rights. America and the other leading democracies backed the idea. The serial abusers did not. In the wrangling at a summit on wider UN reforms last September, Mr Annan's baby was reduced to a skeleton. Many wondered whether it could survive.

Amazingly, it has—just. There is now agreement on the need for a new body, on a par with the Security Council, that would meet several times a year including, when necessary, for emergencies. But its size, powers and composition are still up for grabs. The Americans want no more than 30 members, all with solid human-rights credentials, elected by a two-thirds majority of the General Assembly, along with a routine review of human rights in all 191 UN member states. The abusers want as big a body as possible (to maximise their chance of getting a seat), elected by a simple majority, as at present, with no membership criteria, and no automatic peer review.

Any reform must not just shrink the commission, but must also change the way in which members are elected. At present, regions usually put forward a slate of candidates corresponding to their allotted number of seats, which the General Assembly votes on to the commission as a block. Under one sensible proposal, regions would be required to put forward more contestants than their quota. Each candidate country would then stand separately for election by the General Assembly. Early peer review of all members would further reduce the temptation for thugs

to try to get seats. But opposition is fierce, not only from the most notorious offenders, but also from those middle-ranking ones who fear their relatively minor abuses would be put under the spotlight.

Timing is tight. The old, unreformed commission is due to hold its next annual meeting in March. Mr Annan wants a new one to be ready to take over by then. That means reaching agreement on a blueprint within the next few weeks. If agreement is stymied, the next-best solution will be to wind the existing commission up altogether. Human rights matter too much for the UN to continue to shunt the subject off to a cynical talking shop that has become home to the worst violators. That just blackens the overall reputation of the UN.

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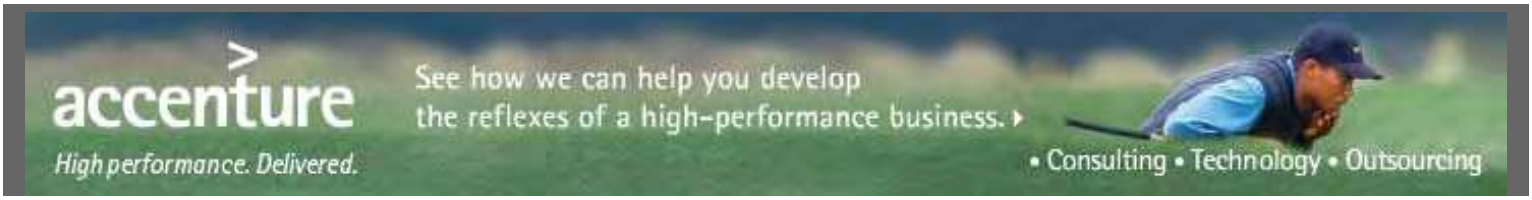
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Spain and its regions

A Catalan kerfuffle

Jan 12th 2006
From The Economist print edition

It is better to talk about rather than just reject demands for more autonomy

WHEN a general talks of the army stepping in to uphold a country's territorial integrity, any democrat should worry. When the country is Spain, which emerged from Franco's dictatorship only 30 years ago and saw off an attempted coup as recently as 1981, the worries should multiply.

That is why Spain's government was right to arrest General José Mena Algado, head of the Spanish army, last weekend, after he said publicly that Catalonia's new constitutional statute, which gives it both more autonomy and recognition as a "nation", might necessitate military intervention. He cited article 8 of the Spanish constitution, which gives the army a mission to guarantee the country's "integrity and constitutional order". The Catalan statute, overwhelmingly approved by the regional parliament last September, is now being debated by the Spanish parliament in Madrid (see article).

Spain's 1978 constitution devolved many powers that were centralised under Franco to the 17 "autonomous regions", though it did so unevenly. The Basque country and Catalonia, which have the most autonomy, have long agitated for more; a sizeable minority in both regions wants to move towards independence. In the Basque case, debate has been disfigured by the violence of ETA, though solid police work has weakened this terrorist group. Yet most governments in Madrid have intransigently refused to consider any more autonomy for the regions, let alone to contemplate eventual independence. The willingness of the Socialist government under José Luis Rodríguez Zapatero, elected in March 2004, to negotiate with the Basque country and Catalonia was a welcome change.

There are respectable arguments against Mr Zapatero's flexibility, even so. Nationalists will never be satisfied by concessions such as a separate judiciary or tax-raising powers; because they always ask for more, it might be better tactically to rule out even limited concessions. Besides, Mr Zapatero's negotiating position is undermined because, in Madrid, his government depends on the votes of left-wing Catalan nationalists; while in Barcelona, the Socialist-led regional government is in coalition with the same nationalist party. Moreover, there is a big financial problem. The Basque country and, especially, Catalonia are among Spain's wealthiest regions. Give them too much fiscal autonomy and they may pull out of the desirable process of transferring money from rich to poor parts of the country. Indeed, a wish to limit net transfers to Madrid has been a driving force behind the new Catalan statute.

Yet Mr Zapatero is still right to favour negotiations. The high-handed refusal of the previous People's Party government, under José María Aznar, even to talk to Basque and Catalan nationalists has merely served to stoke secessionist fervour in both regions. Other countries have discovered that the best way to defuse demands for independence may be to concede more autonomy and even, if need be, to recognise claims to nationhood. Now that they have their own parliament, fewer people in Scotland want a complete break from London. Quebec's demands for independence have to some degree been defanged by Canada's Clarity Act of 2000, which sets out a procedure under which Ottawa would negotiate with any province that votes for independence by a clear majority.

Clarity needed

Because it is the richest part of the country, Catalonia presents more problems than Scotland or Quebec, which are net recipients from central government. Yet since only a minority of Catalan voters seem genuinely to want independence, a bit of pandering to nationalist feeling could still work wonders, even if it involved accepting most of the new Catalan statute and, if necessary, changing Spain's 1978 constitution. Indeed, article 8 of the 1978 text surely needs amendment anyway to remove even the flimsiest excuse for a military intervention. A modern democracy should be capable of accommodating regional autonomy, and even a clear wish for independence. But it

should never be intimidated by a general.

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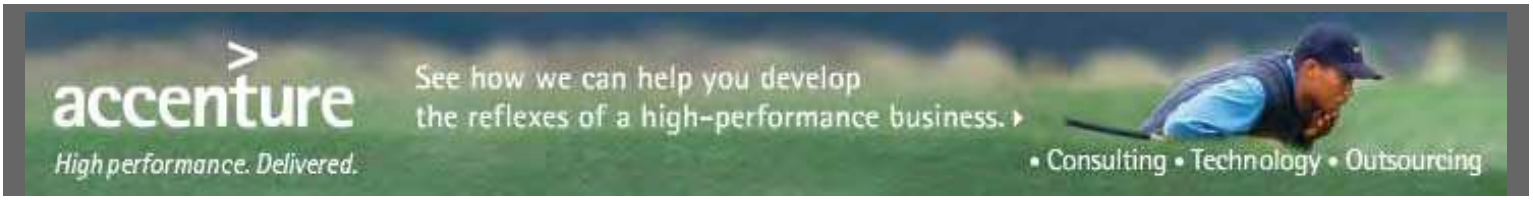
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Walls and fences

From sea to shining sea

Jan 12th 2006
From The Economist print edition

A serious barrier to keep those pesky Mexicans out of the United States

Imagestate

Get article background

BOTHERSOME neighbours? Build a fence. That's what the United States will do if the House of Representatives gets its way. Try as they will, the authorities seem unable to reduce very much the number of people who cross the Mexican border illegally. They are catching more—over 1m last year—but still they come, so the House has voted to put up some 1,125km (700 miles) of fencing—at a cost, it is said, of $2.2 billion.

The Mexicans think this is all rather unAmerican (see article). Whereas Europeans nearly always mark the boundaries of their property with walls or picket fences—and the unsociable British sometimes retreat behind a hedge of *Cupressocyparis leylandii*—friendly Americans often erect no backyard barriers. Yet wasn't it Robert Frost, Yankee to the core, who said good fences make good neighbours? And, anyway, there is a homeland to protect these days. So the border will not be marked by a hedge, nor even a line of cactuses. It will get a proper security fence, complete with lights and cameras.

Don't say it won't work. Congressmen are not stupid. They know that the Maginot line, built to guard France's frontier with Germany, did not hold Hitler up for more than ten minutes in 1940: he simply went round the end. They also know that Germany's counterpart, the Siegfried line, did not perform much better, scarcely delaying the American Third Army at all in 1945. They know, too, that the Scots were wily enough to see that, if they scaled Hadrian's wall and jumped down the other side, they were in England, and the Welsh formed the same opinion about Offa's dyke. They know, too, that China's Great Wall proved no impediment to Genghis Khan when he started his big sweep early in the 13th century. In fact, if you take a trip into space, you may look down and see the remains of pointless walls all over the place—in Greece, Iran or Korea—and, if your eyes are good, you may even discern the remains of Jericho and Troy. Remember what happened to them.

Some of those lines and walls actually did do their job for a while, keeping the hordes back, or forcing them along to some spot where guards could resist them more easily, or just causing a bit of alarm and despondency. Even so, Congress was plainly not inspired by them. It obviously took heart from another, better wall: the “anti-fascist protection structure” put up in Berlin in 1961. It performed pretty well over 28 years, allowing only some 5,000 people to cross it illegally.

If Congress wants its anti-Mexican fence to be as effective, it should take some leaves out of the East German

book. First, forget about lights and cameras; that's Hollywood stuff. Choose instead bunkers, anti-vehicle trenches, lots of concrete and even more barbed wire. Round all that off with minefields, booby-traps, tripwires and machinegun-posts. East Germany was virtually enclosed, so think big: the border barrier will have to be coast-to-coast, 3,200km long, and in the end a fence will not do. It will have to be a wall, as the East Germans discovered. If the Israelis had a bigger budget for their West Bank barrier, they might have gone straight to concrete for all of it, by-passing old-fashioned fencing altogether.

The downside, of course, is on the public-relations front. This just has to be accepted. In fact, all barriers designed to stop people going from one place to another have turned out to be as much about public relations as anything else. That's why China's emperors went on building the Great Wall long after Genghis Khan had shown it to be an utter failure at doing what it was supposed to do. Congress knows that—doesn't it?

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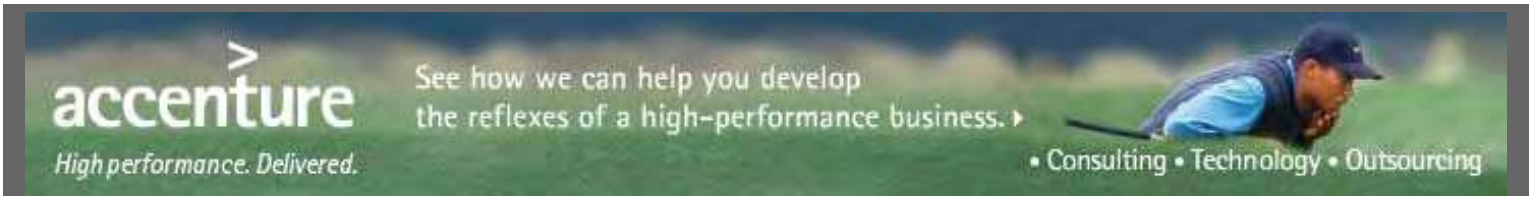
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On France and America, churches' income, student loans, Iraq, junk food, Peoria

Jan 12th 2006
From The Economist print edition

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FAX: 020 7839 2968 E-MAIL: letters@economist.com

Vive la différence

SIR – Your feature on French anti-Americanism left out the quintessential difference between the two countries in terms of political culture ("Spot the difference", December 24th). Whereas the American revolution was driven by Lockean principles (political power is delegated by individuals, constituting a social compact), the French revolution was predominantly inspired by Jean-Jacques Rousseau (individual rights are irrevocably absorbed by government, expressing the *volonté générale* in the shape of majority rule).

Hence, France is still ruled by legal positivism and there is no equivalent to John Locke's notion of the rule of law. Any attempt to limit legislative power by referring to individual rights (the Anglo-Saxon tradition) is deemed anti-democratic and a restraint on popular representation. Attempts to side with the individual in cases of conflict with the collective, such as constitutional limits on taxes and public spending, consistently suffer the bias of "democracy" over liberty.

Jacob Arfwedson
Paris

SIR – Scratch the surface of any problems with the French and you will find the issue of language not far beneath. French was the language of kings and diplomacy until the 20th century and now the French cannot swallow an English-speaking world. Most French officials speak English and studied in British or American colleges. Yet as soon as a microphone appears they switch to French, even if this complicates everything for everyone. It wouldn't surprise me if the French agreed to almost anything, provided it was done in French.

Michael Marchadier
Montreal

SIR – The "dissembling English" who, unlike their revolutionary cousins in America, cannot advocate what their country stands for, may be forgiven their condition. England went through revolutionary traumas over a century before the American war of independence. Indeed, much of the thinking behind the Enlightenment, which you credit as inspiring America's revolution, occurred in England during this period. Having lived through civil war and the beheading of their king, and following the publication of Sir Isaac Newton's "Principia Mathematica" in 1687, the modern world had arrived in England long before those superficial revolutions in their colonies and in France. If "Principia" had been published a century before Oliver Cromwell, England might be a republic still.

Mark Strawbridge
Bristol

SIR – Your article was so long that while reading it I was able to finish a fine glass of Medoc with my *steak frites* at a very fine French restaurant in Brooklyn, down the road from the site of one of the more important battles of the American revolution. The wine was so good that I was indeed able to "spot the difference". The French revolution was fought for the rights of the collective and the state, while the American colonists battled for themselves and the rights of individuals. Give me French wine but American liberty any time.

Vito Racanelli
New York

Religious tithes

SIR – Your report on churches as businesses restated what those of us living in the buckle of the Bible belt have seen happen over the last 20 years ("Jesus, CEO", December 24th). But I must point out that while the delivery system may have been modernised to fit the American corporate model, the concept of using religion to amass riches is as old as the church itself. Just take a tour of the Vatican to see the oldest and most successful multi-level marketing company in the world, a company that aggregates pennies from peasants through a well-structured franchise system so that its CEO (the pope) can live in the most ornate and lavish surroundings. This company is so rich, it even has its own country and laws and does not answer to any secular legal system.

Lee Kleinman
Dallas

Who benefits?

SIR – Although you accurately described the challenges faced by American students who are being burdened by the increase in college tuition fees, your assertion that banks have been receiving a return of 9.5% for student loans is entirely incorrect ("Out of the mouths of babes", December 24th). This piece of misinformation has been frequently advanced by political opponents of the federal government's largest student-loan programme. The fact of the matter is that banks have never received this "egregious" government subsidy because only non-profit and state government-owned student-loan organisations are eligible to issue the tax-exempt bonds that finance the 9.5% loans. Moreover, banks actively support repealing the 9.5% provision and using the savings to increase financial aid. Instead of being unfairly attacked, banks should be recognised for their role in making higher education accessible to all Americans, regardless of family income or background.

Joe Belew
Consumer Bankers Association
Arlington, Virginia

Military precision

SIR – You correctly noted that the United States Army is working diligently and with some success to counter the insurgencies in Iraq and Afghanistan ("How to do better", December 17th). I especially appreciated your references to my book, which argues that the British army was a better learning organisation in Malaya than was the American army in Vietnam. However, I must correct your description of me as "a retired American marine officer". Although I am quite proud of my service under the command of the First Marine Division in Iraq's Anbar province last year, I have never worn the Globe and Anchor. And while some may disagree, I like to think there are still a few good years of active service remaining in these old bones.

Lieutenant-Colonel John Nagl
United States Army
Alexandria, Virginia

Food for thought

SIR – The debate surrounding the advertising of junk food to children neglects one of the strongest influences on any child—their parents' behaviour ("Junior fat", December 17th). Our children's trend towards obesity cannot be reversed without a drastic change in the habits of their role models, which is still some way off considering that the most popular dish in Britain is chicken tikka masala.

Mark Waddington
London

Middling America

SIR – Your article on Richard Pryor credited the phrase, "Will it play in Peoria?", to John Erlichman ("Rebel with a cause", December 17th). According to my grandmother, who has resided in Peoria for 60 years, the catchphrase dates back to the era of vaudeville theatre. To say "it played in Peoria" meant that if a show was a success in this "conventional, boring and safe" town (you certainly hit the nail on the head there), it could run anywhere.

Douglas Hadley
Peoria, Illinois

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CLASSIC
PERTH 2006

Iran's nuclear programme

When the soft talk has to stop

Jan 12th 2006
From The Economist print edition

Now that Iran is crossing a clear red line, what can the world do?

ON JANUARY 10th, Iranian officials removed inspectors' seals and prepared to re-start experiments at the pilot uranium-enrichment plant at Natanz. By doing so, they have sabotaged efforts to deal with Iran's nuclear ambitions by negotiation rather than confrontation. Iran evidently calculates that it will survive the fallout. For the rest of the world, however, its defiance is a critical test.

Crossing the enrichment threshold will not only bring two years of negotiations with Britain, France and Germany to a halt. By ending the suspension of nuclear activities at Natanz that had sustained these talks, Iran has also brushed aside appeals from two of its semi-friends, Russia and China, ignored calls to desist from the 35-nation board of the International Atomic Energy Agency (IAEA), the UN's nuclear guardian, and dismissed pleas from the IAEA's director-general, Mohamed ElBaradei, to do more to build confidence that its nuclear activities are as peaceful as it claims. For if Iran's intentions are not peaceful, and it manages now to cheat on regardless, the credibility of IAEA safeguards and the Nuclear Non-Proliferation Treaty (NPT) these are designed to uphold will be severely damaged.

Shrugging off all such protests, Iran claims that all it will be doing is resuming modest research and development work, and that all it has ever wanted to do is produce low-enriched (up to 5%) uranium (LEU) so that nuclear power stations can help keep the lights on. Indeed, that is so far all the fast-spinning centrifuge machines it is installing at Natanz are configured for. But there are strong suspicions that its nuclear activities—kept secret for 18 years until disclosed by a dissident group in 2002, and declared last November by the IAEA to be in violation of its safeguards commitments under the NPT—have a more sinister purpose.

Iran has no pressing need to start enrichment work now. Pierre Goldschmidt, formerly in charge of safeguards at the IAEA and now a visiting scholar at the Carnegie Endowment for International Peace, recently pointed out that Russia has guaranteed at least ten years' supply of fuel to Iran's single almost-ready reactor, at Bushehr. No other reactors are yet being built, and the fuel-fabrication plant will not be fully up and running until 2012. Yet by experimenting at Natanz, even enriching only tiny quantities of uranium gas, Iran will be learning skills that can be used just as easily to make the highly enriched (90% and over) uranium (HEU) needed for the fissile core of a bomb.

In other words, once enrichment is fully mastered, the only bar to a military programme is intent. Assuming it does want a bomb, how far is Iran from having one? No one knows. But it could soon have several break-out options.

Looking for clues

According to an assessment by the London-based International Institute for Strategic Studies (IISS) in September 2005, by feeding the uranium it produces back through the 1,000 centrifuges it plans to run at Natanz, Iran could take three years to produce a bomb's worth (25kg) of HEU. However, the 50,000-centrifuge commercial plant being built nearby would speed things up a lot. And rather than making its intentions so transparent, Iran could also seek to build up stocks of LEU (the harder part of the enrichment process) for later quick conversion to HEU, possibly at an undeclared enrichment plant elsewhere.

Does Iran have a hidden military programme? Inspectors are unsure. Although they have winkled out a lot of information, the gaps are troubling. Unexplained traces of enriched uranium suggest more “experiments” than have been accounted for so far. Questions remain about what Iran really did with plans it bought on the black market for more efficient centrifuge machines (left gathering dust in a cupboard for years, it says), and whether it used designs it was given by these traffickers for shaping uranium metal in ways useful in weapons-making (no, it insists). Iran has refused to allow full inspection of some military sites thought to be connected with nuclear work, including at least one where high-explosive testing of bomb-triggers may have taken place.

Other evidence adds to this disturbing pattern. For more than a year, America's intelligence agencies have been studying a cache of computer files that appear to show design work by Iranian scientists on a missile cone configured in just the way needed to accommodate a nuclear warhead. Administration officials showed some of this evidence late last year to Russia and China in the hope of winning their active support at the IAEA for declaring Iran in non-compliance with its obligations. (In the end, both abstained on the resolution but let it pass.)

Meanwhile, Iran has long collaborated with North Korea on missile development, testing and deploying its own versions of the North's nuclear-capable Nodong missile, with a range of 1,200km, and possibly collaborating on the longer-range Taepodong missile too. In a forthcoming article in *Survival*, Mark Fitzpatrick of the IISS suggests that such co-operation may recently have extended to nuclear work. Both regimes bought nuclear equipment from the black-market network, run by Pakistan's Abdul Qadeer Khan, which also supplied Libya and others until it was busted. Few other countries would be ready to help Iran with its nuclear projects at present.

The struggle to negotiate

While most governments agree that Iran should not be allowed to build nuclear weapons, if that is indeed its intent (some Iranian officials talk privately of wanting an “option” on a bomb, rather than the bomb itself), it has proved exceedingly difficult to get them to agree on how to stop it. The Europeans first launched their diplomatic initiative in hopes of forestalling more forceful action, either by the United States or by Israel. But the going has been very tough, in part because at first they lacked the full support of some of the bigger players, including America.

That changed early in 2005 when President George Bush decided that, instead of opposing all dealings with Iran, he would throw his weight behind the European effort, albeit without much expectation of success. He also stopped opposing Russia's work on the Bushehr reactor for Iran, having successfully pressured the Russians to insist on return of the spent fuel. The Europeans, now with American and Russian backing, have been offering Iran a package of inducements, including improved trade and political ties and joint work on other less sensitive nuclear projects, if Iran will agree to give up all plans to enrich uranium or make plutonium (another potential bomb ingredient). Given Iran's past lies and evasions, the European three argued, ending all such nuclear work was the only “objective guarantee” that its activities would remain peaceful.

But as America moved to back the European initiative, Iran started to pull away from talks. After the unexpected election of a radical new president, Mahmoud Ahmadinejad, things got even stickier. Last August, Iran restarted its plant at Isfahan that converts natural uranium ore in stages into a gas called uranium hexafluoride that can later be spun in centrifuges. That was already a first breach of its suspension agreement with the Europeans.

Most recently Iran rejected a Russian-backed compromise that would have allowed conversion work to continue, but with the gas converted to LEU on Russian soil and subsequently returned to Iran for use as nuclear fuel. This would have kept Iran from more dangerous nuclear dabbling and so allowed space for talks to continue. But Iran has suggested it would only accept the idea if some enrichment work were to continue in Iran too, which rather negates the point of the exercise.

Has diplomacy therefore failed? The Europeans say they have managed to delay Iran's enrichment work by at least

two years. More important, however, by maintaining a united front among themselves (not always easy), and gaining American and Russian support, they have also managed to focus attention on Iran's obligations under the NPT to observe safeguards commitments and not to seek nuclear weapons, not just the “rights” to fuel-making technologies that Iran claims for itself. And they set out more clearly the lines that Iran (and anyone else with a cloud of suspicion over them) must not cross. But that is why what follows is crucial, now that Iran has chosen to push across one such clear line and restart its enrichment work. Will the Europeans, America, Russia and others call Iran to account, or will they have their own bluff called instead?

A shortlist of options

The first step will be to convene an emergency meeting of the IAEA's board, likely later this month, to receive a formal report about what Iran has been up to. America has long pressed for Iran to be referred to the United Nations Security Council for its actions. Short of an about-face by Iran, the Europeans will now press hard for that outcome. A majority on the IAEA's board already favours referral. But for Iran to take notice, Russia, China and others will have to back the idea too. Both countries have been loth to lean hard on Iran in the past. But both are bitterly disappointed that its regime has upped the ante in this way.

Getting to the council is one thing; getting action from it is another. A presidential statement urging Iran to comply with inspectors' requests, and even assigning the IAEA wider investigative powers, might get through, since the point would be to strengthen the inspectors' hands, not take Iran's case away from them. Beyond that, other steps could include political sanctions, such as denial of visas for sporting teams or for members of Iran's regime (similar actions are thought to have helped in the past in dealing with the recalcitrant Serb government, for example). Unlike the North Koreans, who seem not to mind their isolation, Iranians take pride in their growing contacts around the world and are keen to be accorded the status and respect they feel their ancient civilisation deserves. That said, however, Iran's new president, eager to wipe Israel off the map, seems dangerously unfazed by world opinion (see article).

It would be tougher to win widespread support at the UN for economic sanctions. Several key countries, including Russia (which also recently signed a $1 billion weapons contract with Iran), China, India and Japan have been reluctant to put their oil and gas contracts and their pipeline projects at risk. Yet such targeted sanctions might be the one thing that could get Iran's full attention. Its energy industry is dependent on foreign investment for future expansion and modernisation. Meanwhile, India is an important supplier of refined petrol to Iran.

The Europeans have already hinted that if sanctions are blocked at the UN, they will impose their own. They will also try to get others to join them, rather as America has orchestrated the Proliferation Security Initiative, an informal posse of countries prepared to take tough action to block shipments of illicit goods and materials around the world related to weapons of mass destruction.

The last resort

Might force be the answer? Mr Bush has always said that no option is off the table. Israel says Iran must not be allowed to develop nuclear weapons and has suggested that, once Iran has mastered enrichment, perhaps as early as a few months from now, its nuclear programme will have passed “the point of no return”. Might either government be tempted to pre-empt the diplomacy with military strikes?

Israel's air force flattened Iraq's Osiraq nuclear reactor in 1981. But Iran has learnt from that episode. It has dispersed, hidden and buried its numerous facilities; some sites, including Natanz, are up to 75 feet underground. Nor is sabotage much of an option. Ploys such as assassinating Iranian nuclear scientists or infecting Iranian computer systems with viruses would cause minimal damage. And yet there are military options, however imperfect and risky.

Only America could hope to demolish Iran's programme. The Iranians are believed to have, in addition to its main sites, at least a score with a role in the programme, and more than 100 sites suspected of having a role. To attack them all, with cruise missiles and fighter-bombers, would require an extended campaign and hundreds of sorties. Corridors would have to be cleared through Iran's air defences and the Iranian air force destroyed. Collateral damage, to Iranian civilians and cities, could be extensive.

A likelier alternative might be to launch an attritional campaign by attacking Natanz and Bushehr, recognising that the resulting damage would at best delay Iran's nuclear progress. This is certainly the most that Israel could contemplate unilaterally. Such an attack would be a declaration of a war which Israel could start but might not be able to finish without American protection. And Israeli fighter-bombers would find it hard to reach Iran without passing through American-controlled airspace.

To attack Iran this way would make sense only if it were thought likely that a friendlier Iranian regime would then emerge. But Iran has no obvious, friendly government-in-waiting. And Iran could strike back—by closing the oil chokepoint of the Strait of Hormuz or hitting American or Israeli interests via proxies in Saudi Arabia, Iraq, Lebanon and the occupied West Bank and Gaza. Israel is well within range of Iranian missiles. Diplomacy has not stopped Iran so far. But military action is by no means an attractive alternative.

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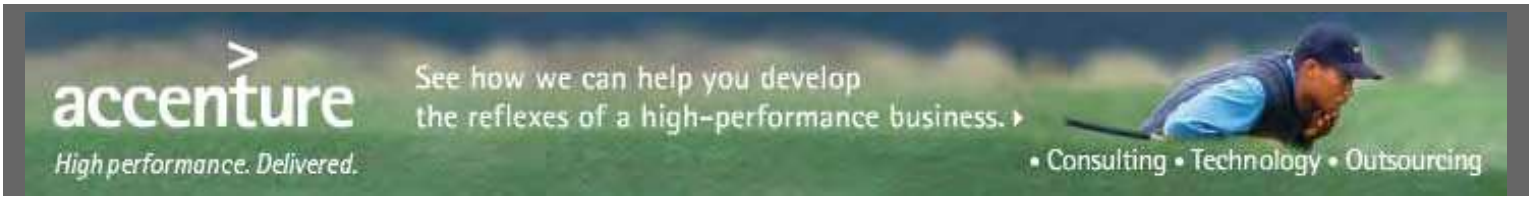
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Iran's psychology

Whistling in the gloom

Jan 12th 2006 | TEHRAN
From The Economist print edition

Rightly or wrongly, Iran feels a glow of immunity

AS THE snow falls in Tehran, the surreal shape of Iran's public diplomacy shows through the gloom. Unfazed by the determination of some European countries to prevent the Islamic Republic from developing a nuclear fuel cycle, Ayatollah Ali Khamenei, the supreme leader, hopes those same countries may invest in the project.

Between expressions of hope that Ariel Sharon, Israel's incapacitated prime minister, will die soon, Mahmoud Ahmadinejad, Iran's president, has offered to dispatch officials to help EU countries solve their human-rights problems. As is often the case with obscure signals in a blizzard, the world pays little attention.

Do Iran's leaders underestimate the determination of America and its allies to punish them for persisting in their nuclear plans? In public, Mr Khamenei nonchalantly recalls that past sanctions against Iran—which peaked when he was president in the 1980s, during a crippling war against Iraq—actually helped to generate self-reliance. But Mr Khamenei has built a reputation for canny politics on the implicit understanding that Iranians are no longer the privation-seeking revolutionaries they once were. Doveish citizens pin their hopes on his well-documented tendency to pull back from the brink of major confrontation. For all that, he does not like to be outmanoeuvred by hawks, and Mr Ahmadinejad is being serially provocative.

The president probably had little say in the decision to restart research at Natanz. All the same, his repeated rhetorical excesses and the anger they have provoked make it hard for any Iranian leader—least of all one, such as Mr Khamenei, who has a small natural constituency among Iranians—to climb down without being accused of betrayal. Some Iranian analysts contend that Mr Ahmadinejad's bellicosity serves Mr Khamenei's purpose, because it reminds Israel and America that any military action against Iran will not go unanswered.

The Iranians believe that America's parlous position in neighbouring Iraq, and Israel's vulnerability to the rockets of Hizbullah, a militant group based in southern Lebanon and backed by Iran, militate strongly against an attack. But it is the high price of oil that most bolsters a sense of immunity in Tehran. In the 1990s, Iran made do with oil-export revenues worth an average of around $15 billion a year; by contrast, projected revenues for the current Iranian year are a whopping $50 billion. While energy prices remain high, Iran's leaders believe, and all Iranians hope, that the world will not dare boycott Iranian oil.

The nuclear issue is given less coverage in Iran's media than you might expect; recently, editors have allotted more space to arcane disputes over the nature of clerical rule. And for the authorities the country's sensitive circumstances are an excellent excuse to delay relaxing pressure on pro-democracy forces.

When they are asked, many Iranians profess to support the government's pursuit of nuclear technology. Some liken the West's attitude to Britain's and America's unhappiness at the nationalisation of Iran's oil industry in the 1950s. (The prime minister who did the nationalising was subsequently unseated in a CIA coup.) Others hope that their leaders are indeed in pursuit of a nuclear weapon; several neighbours have them, including Israel and Pakistan. But it is unlikely that many would willingly endure a reprise of the economic isolation of the 1980s. For all the pyrotechnics of his president, Mr Khamenei's path is a narrow one.

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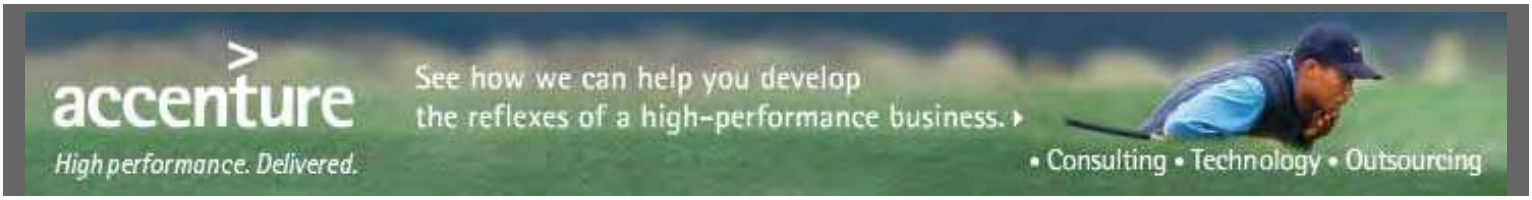
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The Supreme Court

The brainbox and the blowhards

Jan 12th 2006 | WASHINGTON, DC
From The Economist print edition

Getty Images

Samuel Alito, George Bush's latest pick for the Supreme Court, faces a tough and dirty battle for confirmation. But he looks as though he'll win

Get article background

TED KENNEDY is deeply troubled by the ethics of the Supreme Court nominee. Between 2001 and 2006, Samuel Alito, who is currently an appeals court judge, accepted $7,684,423 in “donations” from special interests who perhaps wanted the law tweaked in their favour. That included $28,000 from defence contractors, $42,200 from drug firms and a whopping $745,373 from lawyers and law firms.

No, wait. Those are Senator Kennedy's conflicts of interest—or, rather, a brief excerpt from a long list compiled by the Centre for Responsive Politics. The lapse for which the senator berated Mr Alito was considerably less clear-cut.

To avoid conflicts of interest, Judge Alito invests most of his savings in mutual funds, rather than individual firms that might appear before him. He does it through an investment company called Vanguard. Though no rule required this, he promised, when nominated to the appeals court in 1990, that he would disqualify himself from cases involving Vanguard. Twelve years later, such a case came up, but he forgot to recuse himself. When he realised his mistake, he recused himself from a fresh appeal. No one claims that he stood to benefit from his judgment.

That the Democrats on the Senate Judiciary Committee are giving him a hard time about Vanguard shows how high the stakes are. If confirmed, Mr Alito would sit for the rest of his life—and he is only 55—on the court that struck down segregation, legalised abortion and made George Bush president in 2000. The seat he seeks to fill is that of its retiring swing voter, Sandra Day O'Connor. If he is as conservative as one expects a Bush nominee to be, he would shift the court significantly rightwards.

So one would expect senators to ask him tough questions. Instead, most chose to make speeches. On the second day of hearings, ten out of the first 12 senators spoke for longer than the nominee. Patrick Leahy of Vermont waxed thespian on the subject of strip-searching young girls, a practice of which he said Mr Alito was too tolerant. In one burst, he rolled the words “strip-search” around his mouth four times and “ten-year-old girl” five times.

Judge Alito, when he could get a word in edgeways, explained that in the case in question, police officers asked a magistrate for permission to search everyone in a suspected drug dealer's house, since they had cause to believe he hid his wares on other people. The officers got a warrant that they thought authorised this, but which lawyers subsequently argued didn't. The suspected dealer's wife and daughter were searched by a female officer. No drugs were found. The officers were sued. Judge Alito voted to dismiss the suit, arguing that the officers had reasonable grounds to think the search was warranted.

Activists on the left say Judge Alito is a far-right ideologue. They gripe that Democratic senators were too soft on the last Bush pick to appear before them. John Roberts was confirmed as chief justice last year by 78 votes to 22, after a performance even his foes admit was brilliant.

Judge Alito cannot match the polish of Chief Justice Roberts, who spent most of his career as an advocate before the Supreme Court, and is therefore practised at swaying the powerful. Judge Alito seems shy and bookish—his wife, a former law librarian, says it took him 13 months to ask her out. When he first appeared before the Senate, he was so nervous he was briefly struck dumb. But he soon found his stride, because he clearly knows more about the law than his inquisitors do.

His record on the bench is one of cautious rulings and scrupulous deference to precedent

Even a cursory look at his record shows that the sound-bite charges against Judge Alito—that he doesn't think machineguns should be regulated, that he never sides with blacks alleging discrimination—are simply untrue. His record on the bench is one of cautious rulings and scrupulous deference to precedent.

Take the case of *Planned Parenthood v Casey*. In 1991, he argued that a Pennsylvania law requiring women to notify their husbands before having an abortion was constitutional. The law did not require women to ask their husbands' permission, and they could escape it entirely if they said they feared their husbands might beat them up. Referring to a standard laid down by Justice O'Connor, Judge Alito argued that this did not place a “severe limitation” on a woman seeking an abortion.

His colleagues disagreed, as, later, did the Supreme Court. The National Organisation for Women says this makes him a “fanatical anti-abortion judge”. The judge's defenders retort that he was more faithful to Justice O'Connor's precedent than she herself was. In her ruling on *Casey*, she changed the standard from “severe limitation” to “substantial obstacle”.

That, however, is a Supreme Court justice's prerogative. If Judge Alito is confirmed to the highest court, he, like his predecessor, will no longer be bound to follow its precedents. His long record of careful, restrained rulings on the appeals court suggests that he will not abuse this power, but it does not guarantee it.

Of the many areas where Judge Alito's views will matter, two stand out: abortion and executive power. It would take five votes on the Supreme Court to overrule *Roe v Wade*, the 1973 decision that barred states from banning abortion. Two are assured. Two are unknown, including Judge Alito's. But there is solid evidence that he thinks *Roe* was wrongly decided—he said so in an application for a job in the Reagan administration in 1985.

Probed repeatedly on the subject this week, the judge refused to say how he would rule on *Roe*. He said it was important, in general, to let precedents stand, but admitted that this was not an inviolable rule. (Were it so, segregation would have lasted longer than it did.) If the case were to come before him, he said, he would approach it “with an open mind”.

Given the controversy over Mr Bush's stance on torture and warrantless wiretapping, the issue of executive power is even more topical (see article). Mr Kennedy suggested that Mr Bush only nominates judges he thinks will defend “the most expansive view of presidential authority” and that Judge Alito's views on the subject are of the sort that “most Americans find disturbing and even frightening”.

The evidence for this is scanty, but Judge Alito's responses will not reassure those who believe, as Mr Kennedy put it, that the White House is abusing power, authorising torture and brazenly infringing the civil rights and liberties of the American people. The president, said Judge Alito, is always bound by the law, especially during times of war when the temptation to flout it is greatest. But he wouldn't say whether he thought Mr Bush has broken the law in particular instances, because that would prejudge cases that might well come before him. It is a sound argument, and nominees always use it, but it leaves everyone in the dark.

A vote is scheduled for January 20th. With Republicans holding 55 of the Senate's 100 seats, Judge Alito will be confirmed unless the Democrats opt to filibuster. That would be politically unwise. There is little evidence voters buy the idea that Mr Alito is an extremist. And on the basis of the hearings so far they are right.

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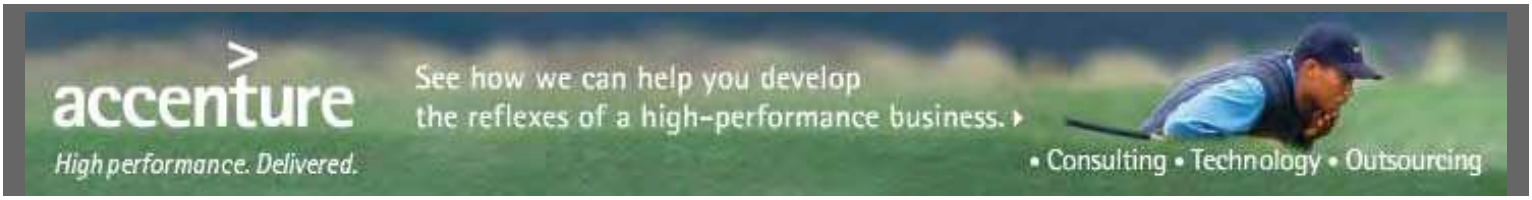
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School choice

Why judges matter

Jan 12th 2006 | WASHINGTON, DC
From The Economist print edition

AP

They can protect defunct monopolies and mess up children's lives

Get article background

JEFFREY LEWIS didn't learn much at the Booker T. Washington high school in Miami. “There was a lot of fighting,” says his mother. If the teachers “tried to do anything, someone interrupted. By the time [the students] got through talking about their brand name [clothes], it's another period,” she maintains. “It wasn't a school, just a place to hang out.”

Bright but shy, Jeffrey kept his head down and got Ds and Fs. But then, using a voucher scheme aimed at helping Florida children escape from failing inner-city schools, he moved to a private school, where his grades are now excellent. Unfortunately for him, the Florida Supreme Court last week struck down the voucher scheme that rescued him.

Florida's state constitution guarantees a “uniform, efficient, safe, secure and high quality system of free public schools”. Low-quality inner-city schools would appear to violate this guarantee, but when the state's governor, Jeb Bush, tried to offer parents an alternative, the teachers' unions sued—and the judges ruled in their favour. The state's “Opportunity Scholarship” programme, wrote Chief Justice Barbara Pariente, is unconstitutional because “it diverts public dollars into separate private systems parallel to and in competition with the free public schools.”

That, of course, is the point. Vouchers not only offer better education more cheaply to the children who receive them; they also force rotten public schools to improve, by pinching their students if they don't, as at least four studies in Florida have shown. For Justice Pariente and her colleagues, however, what matters is not that public schools be any good, but that they should remain a monopoly.

Voucher opponents rejoiced, but not ecstatically. “It hardly seems like a victory,” said one union leader, before demanding higher salaries for his members. The ruling affects only the smallest of Florida's school-choice programmes, serving a mere 700 or so students. Two larger programmes appear safe, for now: one because it is funded by tax credits rather than vouchers, and the other because its beneficiaries are disabled, which the court said meant they should be left alone.

Nationally, and despite constant legal attacks, vouchers are spreading. The Alliance for School Choice called 2005 the “best year ever” for new legislation, with six states enacting new programmes or extending old ones. Some 130,000 children are expected to benefit directly this year, excluding the 370,000 theoretically eligible under a federal bill aimed at those displaced by Hurricane Katrina.

Out of a total of 55m schoolchildren, however, this is a drop in the inkwell. Supporters now worry that other states whose constitutions require “uniform” schools will follow Florida's route, though Wisconsin and Ohio have already rejected similar arguments. And there is still the thorny issue of whether parents can use vouchers to send their children to religious schools—as many want to.

The United States Supreme Court ruled, in 2002, that this did not violate the constitutional separation of church and state. But most state constitutions, including Florida's, include “Blaine amendments”, originally tools to keep Catholics down, which go further than the federal constitution in barring the use of public funds in religious schools. Such clauses have already been used to thwart choice in Vermont and Puerto Rico.

The Florida court has graciously allowed Jeffrey Lewis and his fellow opportunity scholars a grace period, until the end of the school year, before they are tossed back into their old schools.

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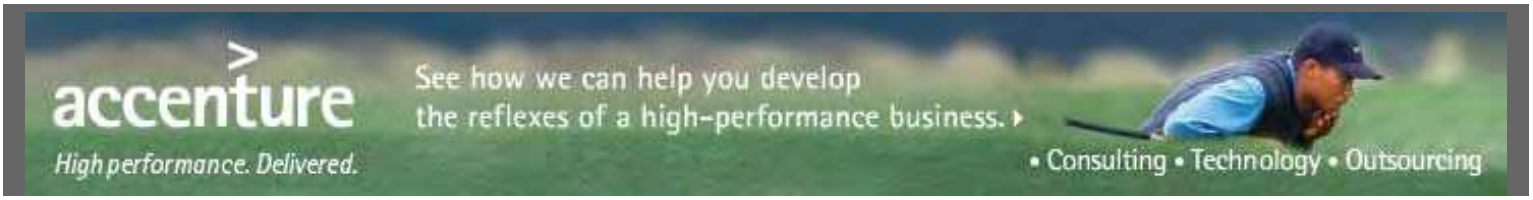
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No DeLay

Time for a proper fight

Jan 12th 2006 | WASHINGTON, DC
From The Economist print edition

The Republicans face an important succession battle

AP

Blunt, climbing upwards

SO THE Hammer has finally fallen. Unable to shrug off a campaign-finance indictment in Texas and mired in the growing scandal surrounding Jack Abramoff, the disgraced super-lobbyist, Tom DeLay has decided to give up his attempts to regain his job as majority leader. A high-octane era of Republican politics has ended; and a struggle for succession has begun that could determine whether the party regains its reforming momentum.

Mr DeLay's successor will have to grapple with three big questions. First, do you stick to the Hammer's hard-charging brand of politics, riding roughshod over the opposition? Mr DeLay is one of the most impressive fundraisers in Republican history, as well as a canny (and brutal) vote-counter; many people could not copy him even if they wanted to. Second, how can you shield the Republican Party from the Abramoff fallout? Some want to treat the disgraced lobbyist as just a bad apple; others think his case raises tough questions about the right's links to money politics. Third, how do you lead the party into this year's mid-term elections? There is a clear danger of the conservative factions tearing each other apart: how do you restore some momentum and esprit de corps?

Big questions all. But the two men who so far have put themselves forward to answer them look decidedly small. The front runner, Missouri's Roy Blunt, is a DeLay protégé: the Hammer without the heft. Mr DeLay levered him into his current position, as majority whip, but Mr Blunt is not as good as his master at managing the House floor. Like Mr DeLay, he has no interest in ideas but plenty of close contacts with K Street, the boulevard of boondoggles at the heart of Washington. He even tried to insert a provision helping a tobacco firm into the bill setting up the Homeland Security Department.

Ohio's John Boehner is hardly more inspiring. He rose to a leadership position during the heady days of the Newt Gingrich revolution (he was ousted in 1998 along with his boss). And he has a commendable record of shaping big education and pension bills. Mr Boehner has released a 37-page manifesto arguing that his party is “stuck in neutral and hesitant to push the accelerator”. But is Mr Boehner the right man to put his foot down? He also has close ties to K Street and a taste for fancy golf resorts and corporate jets. In 1995 he raised eyebrows by distributing campaign cheques from tobacco lobbyists on the House floor.

The White House is worried that the leadership contest, which is scheduled to start after George Bush's state-of-the-union address on January 31st, will distract attention from the president's policies. It will also put a question-mark against Mr Bush's ability to push anything through Congress: whatever folk said about Mr DeLay, he got things done.

In fact, the real problem with the election contest is not that it will roil conservative waters but that it won't roil them enough. The fact that the field is so weak speaks volumes about the mood of complacency in the Republican Party. A few people—such as Indiana's Mike Pence and Arizona's Jeff Flake—seem to grasp the seriousness of the situation, but not enough to risk a leadership bid. Most Republicans think they can just muddle through. Forget that 58% of Americans think that the Abramoff case is evidence of “widespread corruption in Washington”. Forget that most Americans think that corruption will be an important voting issue come November. And forget that the current scandal will only grow as Mr Abramoff spills the beans. The Republicans are so addicted to the perks of incumbency that they are reluctant to change the status quo.

To be fair, their complacency is justified on one count: the uselessness of the opposition. Nancy Pelosi has proved

a disastrous minority leader—a San Francisco leftie who is out of tune with the heartland and a lacklustre party manager who can't keep her caucus in order. The Democrats' high command is dominated by old committeemen who, in other walks of life, would have long ago retired; John Dingell, of the Energy and Commerce Committee, is 79 and Tom Lantos, of the International Relations Committee, is almost 78. Thanks to Mr Abramoff, the Democrats have their best chance in years of shaking up American politics. They may well fluff it.

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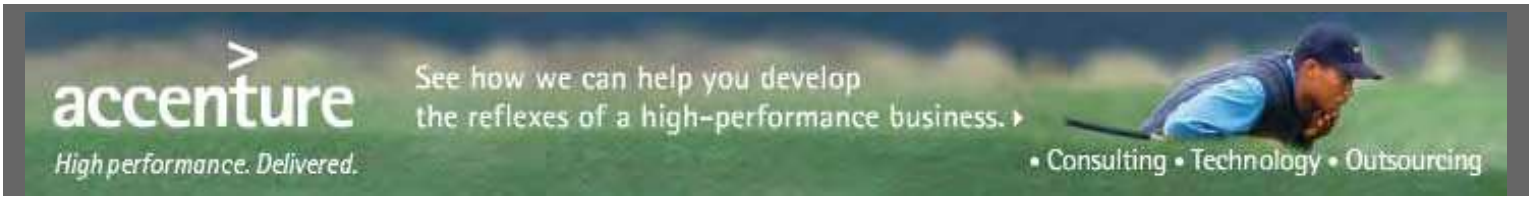
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A spending splurge in California

Build it

Jan 12th 2006 | LOS ANGELES
From The Economist print edition

Despite the odd tumble, the governor has discovered his inner Pat Brown

ARNOLD SCHWARZENEGGER once made his living as a bricklayer, which perhaps explains his new mantra. He used the words “build it” seven times in last week's state-of-the-state address, where he unveiled a ten-year plan to invest some $223 billion to upgrade the tired infrastructure of the world's eighth-biggest economy. That was arguably the biggest splurge since the 1960s under Governor Pat Brown, a Democrat; and this week Mr Schwarzenegger followed it up with a budget for the year beginning in July that showers money on state services.

Is this credible from the man who promised to tear up the state's (famously overextended) credit card? In political terms, it probably is. Two months after his humiliation in a special election, when the voters rejected all four ballot propositions he had sponsored, the governor is back to his old confident self, even shrugging off a motorcycle accident that left him with a bruised lip and the painful realisation that he has been riding his Harley for years without a proper licence.

Most Californians want to see more money spent on their infrastructure. A promise to build 1,200 miles (1,931km) of new highway lanes, 600 miles of new bus and rail routes, two new prisons, 101 new courts and 40,000 new classrooms makes intuitive sense to an electorate fed up with gridlocked traffic, pot-holed freeways, gang crime and poor public schools. So, too, in the wake of Katrina, does the idea of upgrading the levees in the flood-prone north of the state.

The booming economy has also given the governor more room for manoeuvre in the short term as well. Having found an extra $7 billion in unexpected tax revenue, the governor is proposing to spend $125.6 billion in the fiscal year beginning on July 1st; the general fund will rise by 8.4% to $97.9 billion. Welfare will be cut, but now university fees will not need to be increased. There will be more cash for schools, medical services for 300,000 uninsured children and even an increase in the minimum wage from September, from $6.75 an hour to $7.25.

The governor's director of finance, Michael Genest, insists this is manageable. The state's structural deficit—some $14 billion in his boss's first budget, for 2004-05—will be $4.7 billion in 2006-07 and probably disappear altogether in 2007-08. As for the ten-year plan's $223 billion price-tag, some 70% of that will come from the private sector and the federal government. The rest will come from $68 billion in taxpayers' bonds. And Mr Schwarzenegger is proposing a constitutional amendment to ensure that debt service on the bonds can never exceed 6% of the general fund. So the package is more like taking out a mortgage to rebuild your house than running up your credit-card bill.

The details could be tricky. The governor is asking the legislature to approve the entire ten-year plan as a single package, and the bonds—perhaps some $25 billion-worth this year—need to be approved by the voters too. But for the moment, at least, Mr Schwarzenegger has wrongfooted his opponents on both sides of the aisle.

Conservative Republicans, cross about a surge of liberals in the governor's office since the November debacle, may blanche at the idea of increasing the state's debt; but Mr Schwarzenegger is also refusing to raise taxes. As for the Democrats, they find it hard to criticise the long-term plans of a Republican so clearly trying to imitate Governor Brown, who built much of the state's current infrastructure in the 1960s.

Phil Angelides, the state treasurer who is running against Mr Schwarzenegger in the November election, sniffs that the plan is all hype and phoney numbers. The voters have approved bonds worth $42 billion over just the past six years, and much of the money is not “new” at all, but would have been spent anyway on building roads and schools.

Mr Schwarzenegger will not be too worried by Mr Angelides's carping. California—home to both Hollywood and Google—has always liked big ideas. And it needs them now that its population is set to rise by 30% in the next 20 years, the equivalent, says the governor, “of adding three new cities the size of Los Angeles”.

More important, Mr Schwarzenegger returned to the “Republican-lite” style that made him so popular in his first year. Like a movie that went straight to video, the right-turn last year that saw him try to bash the unions and cow the legislature is now forgotten: “the people sent a clear message—cut the warfare, cool the rhetoric, find common ground and fix the problems together. To my fellow Californians, I say ‘Message received’.” If only they had said something about motorcycles too.

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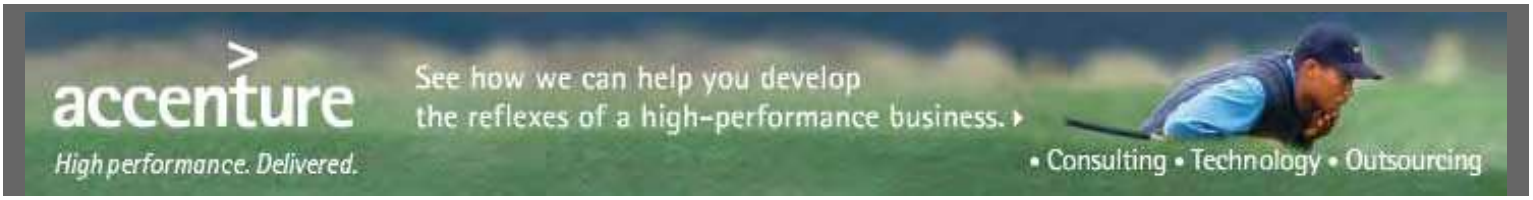
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Tax policy

Tripe is back on the menu

Jan 12th 2006
From The Economist print edition

Alas, the White House has returned to a one-note fiscal policy

A YEAR ago, it seemed possible that George Bush's second term might produce fiscal reforms that would atone for some of the profligacy of the first four years. The serial tax-cutter and big spender would reform the Social Security pensions system and overhaul the tax code.

Long before 2005 ended, it was obvious that Social Security was going nowhere. Now tax reform seems to have gone too. It will be lucky if it gets a mention in the state of the union address on January 31st.

Instead Mr Bush has returned to the tried and tested: boosterism about the benefits of tax cuts. Listen to his recent speeches and the economic agenda seems to have three goals. First, convince Americans that the economy is actually doing well. Second, credit all good economic news to the tax cuts. Third, push hard for making the existing tax cuts permanent.

No one can blame an embattled administration for focusing on the surprisingly buoyant economy. For instance, Mr Bush is not the first president to try to grab the credit for good economic news, ignoring the role, for instance, of low interest rates. The real chutzpah lies in the degree to which the Bush team claims that tax cuts are the cause of the economy's strength.

The past 18 months, we are told, offer clear proof that the entrepreneurial spirits unleashed by lower taxes boosted investment, productivity and the stockmarket. In May 2003, the administration pushed through a package accelerating cuts in income taxes and slashing taxes on dividends and capital gains; soon afterwards investment and output growth shot up. “Business investment literally turned around overnight when those tax cuts took effect,” the treasury secretary, John Snow, crowed this week. Dick Cheney joined in. “It's getting pretty hard for the critics to make the case that somehow those tax cuts weren't good for the economy,” argued the vice-president.

A surprising rise in tax revenue last year has pushed this chutzpah even further. Mr Bush last week implied that the supply-side fantasy might hold after all: tax cuts do pay for themselves. “There's a mindset in Washington that says, you cut the taxes, we're going to have less money to spend,” he noted contemptuously, before claiming that recent experience suggested otherwise.

Mr Bush is back to the pabulum that tax cuts in any shape spell prosperity

Even by the standards of political boosterism, this is extraordinary. No serious economist believes Mr Bush's tax cuts will pay for themselves. A recent study from the Congressional Budget Office suggested that, after ten years, up to one-third of the cost of a 10% cut in income taxes can be recouped from higher economic growth. That fraction may be higher for cuts in taxes on capital alone. But it is nowhere near 100%. What is true is that the timing of temporary tax cuts can affect revenues temporarily. Thus, a chunk of last year's surge in corporate tax receipts was thanks to the expiration of the temporary investment incentive in 2004.

Academic analysis on the impact of the 2003 tax cut is sparse. A study by Matthew Shapiro and Christopher House from the University of Michigan suggests that the temporary investment incentive did raise output by a modest 0.1% during 2003 and 2004. Studies by Raj Chetty and Emmanuel Saez from Berkeley show that the dividend tax cut prompted firms to pay more dividends, but whether it boosted share prices is more controversial. A study by Alan Auerbach from Berkeley and Kevin Hassett of the American Enterprise Institute suggests it did; another paper by economists at the Fed claims not. There is little evidence that the dividend tax cut boosted investment. Even in theory, economists are unsure about how much lower dividend taxes boost investment directly.

So the Bush team is clearly overstating its case. That is galling given the president's apparent retreat from tax reform. After all, a president who really believed in the importance of a pro-growth tax code would be pushing for an overhaul; he would also admit that a more efficient tax code would create losers as well as winners. Instead, Mr Bush is back to the pabulum that tax cuts in any shape spell prosperity.

Worse is the refusal to acknowledge the unsustainability of today's fiscal mix. Mr Bush still blathers about halving the deficit by 2009, but the administration's forecast assumes no reform of the Alternative Minimum Tax and it consistently underestimates the cost of the war in Iraq. A new paper, by Joseph Stiglitz of Columbia and Linda Bilmes of Harvard, claims that the total budgetary cost of the war could exceed $1 trillion.

That is debatable; less so is the dire long-term fiscal outlook, once baby boomers begin to retire at the end of this decade. Either entitlement programmes, such as health and pensions schemes for the elderly, must be reformed, or taxes will have to rise. Mr Bush will surely not get the first done. And he seems set on digging the tax hole still deeper.

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Presidential power

Under challenge

Jan 12th 2006
From The Economist print edition

The courts and Congress are beginning to rein in Mr Bush's presumed powers as commander-in-chief

Get article background

MOST presidents like to try and expand their powers. But in repeatedly invoking his constitutional authority as commander-in-chief in the “war on terror” to bypass both domestic laws and international treaties, George Bush has taken the art to new heights. Now a backlash is under way, with both the courts and Congress overcoming their traditional deference to the executive in wartime.

Two congressional committees have set up inquiries into Mr Bush's authorisation of a secret domestic spying programme without warrants. Another has announced its intention of “monitoring” the administration's implementation of a new ban on the use of torture that the president seems bent on sidestepping. And this week senators grilled Judge Samuel Alito, Mr Bush's new pick for the Supreme Court, about his attitude to executive power.

Meanwhile, the court is considering holding hearings on the president's claimed wartime authority to detain terrorist suspects indefinitely and without charge. Earlier this month, while backing the administration's right to transfer José Padilla, an American citizen, from military custody to face trial before a civilian court in Miami, it reserved the right to examine “in due course” Mr Padilla's broader claim that Mr Bush overstepped his authority in holding him for more than three years without charge as an alleged “unlawful enemy combatant”.

Mr Padilla's transfer had been denied in December by the normally conservative Fourth Circuit Court of Appeal. In a sign of impatience, it lambasted the government for using one set of arguments to justify Mr Padilla's continued military detention and another to persuade the Miami grand jury to indict him. Judge Michael Luttig was particularly scathing about the apparent ploy of putting Mr Padilla on trial in order to avoid the broader issue of enemy combatants going to the Supreme Court.

The administration said this was “an unwarranted attack on the exercise of executive discretion”. It used the same stock argument against Senator John McCain's bill banning the “cruel, inhuman and degrading treatment” of detainees by Americans anywhere in the world. And even though Mr Bush eventually gave in to the public outcry on this issue, it has now emerged that at the very moment of signing the bill into law the president quietly issued a statement reserving his right to flout it: “The executive branch shall construe [the law] in a manner consistent with the constitutional authority of the president...as commander-in-chief.”

A furious Mr McCain, who is due to take over as chairman of the Senate Armed Services Committee, has said the committee will monitor the law's implementation closely. Suspicions about Mr Bush's intentions have been aggravated by the recent row over the CIA's use of “extraordinary rendition” to transport terrorist suspects to third countries for interrogation; but they also date back to the infamous “torture memos”, leaked in 2004, where administration lawyers claimed the president could approve any interrogation technique he believed necessary to protect the nation's security.

Since then, the White House has retreated, dismissing the memos as “a scholarly effort to define the perimeters of the law”; it has also broadened its shockingly narrow definition of torture. But it has not retreated from the notion that the president's wartime powers mean he can do what he sees fit.

Mr Bush is not the first to claim the right to override treaties and laws in time of war. Abraham Lincoln suspended the right of habeas corpus during the civil war, and thousands of Japanese-Americans were detained without charge in the second world war. But with the return of peace, habeas corpus was restored and the internees

released. The problem with Mr Bush's war on terror is its unending nature. He himself has said it will last “until every terrorist group of global reach has been found, stopped and defeated”.

All the same, it is hard to find anyone nowadays who thinks Mr Bush's powers are unrestricted. This week, Mr Alito said the president does not have a “blank cheque”, even in wartime. Dick Cheney, the most ardent defender of executive power, recently claimed (with a straight face) that Mr Bush “has made clear from the outset, both publicly and privately, that our duty to uphold the law of the land admits no exceptions in wartime.”

The vice-president's claim might be justifiable if you believe that the commander-in-chief clause of the constitution trumps all other laws. But this is precisely what others are now beginning to challenge.

There is a legal precedent. In 1952, during the Korean war, the Supreme Court was asked to rule on whether Harry Truman had the right to order the seizure of the nation's steel mills without consulting Congress. It decided he did not. His power as commander-in-chief, argued Justice Robert Jackson, was at its strongest when he acted pursuant to congressional authorisation. But “when the president takes measures incompatible with the expressed or implied will of Congress, his power is at its lowest ebb.”

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Guns to the left, guns to the right

Jan 12th 2006
From The Economist print edition

The Clinton restoration project is under fire from both sides

THERE are few greater political assets than the idea that you have history on your side. George Bush rode the good horse “inevitability” to the Republican nomination in 2000. And Mrs Clinton hopes to ride the same horse to the Democratic nomination in 2008. But can she pull it off? Can the Clinton dynasty bridle history as successfully as the Bush dynasty? That is one of the most intriguing political questions of the next two years.

The similarities between Mrs Clinton's position today and Mr Bush's eight years ago are striking. Mrs Clinton enjoys the same advantages as the Texas-governor-turned-presidential-candidate—from an overflowing war-chest to support from every established faction of her party. (Who else can claim to have a chunk of organised labour and the Democratic Leadership Council in their pocket?) But look more closely at these similarities and you discover that they conceal intriguing differences—differences that do not help the Clinton restoration project.

Start with Mrs Clinton's new-found enthusiasm for centrism. The junior senator for New York is following exactly the same strategy as the former governor of Texas—exploiting her celebrity to vault over the pander-fest of the party primary and instead run as a centrist from the beginning. Just as Mr Bush once ran, in those far-off days, as a “compassionate conservative” and a “uniter not a divider”, so Mrs Clinton is running as a war hawk and a New Democrat. She has been steadfast in her support of the Iraq war—and has even argued for sending 80,000 more troops. She is such an active member of the Senate Armed Services Committee that the Pentagon has invited her to join a special panel on rethinking defence. She has denounced violent video games and called abortion “a tragic choice”. And she has gone out of her way to co-operate with Republicans (such as Newt Gingrich and Rick Santorum) who once regarded her as the spawn of Satan. The *National Journal* ranks her as one of the seven most conservative Democratic senators on foreign policy—and one of the 14 most conservative on policy *tout court*.

But Mrs Clinton's job is proving much harder than Mr Bush's was. Her strategy was based on the assumption that she had the left under her thumb: that she had enough capital as both a feminist icon and a victim of the vast right-wing conspiracy to move to the centre with impunity. Two things have upset that plan.

The first is the furore over the war in Iraq. Many Democratic activists regard the war as such an abomination—an act of aggression justified by lies and driven by greed—that they cannot have any truck with someone who

supports it, even a liberal martyr. The second is the rise of the so-called “netroots”. Mrs Clinton may have the traditional feminist and labour groups in her pocket, but the internet is devolving power from client groups to local activists. The internet left is in open revolt against the Washington establishment, and it looks back on the Clinton presidency not as a triumph that should be repeated but as an error that should be avoided—a time when the party gave in on welfare and public spending and lost control of Congress.

It would be foolish to underrate Mrs Clinton

Mrs Clinton will probably face a much more formidable field of competitors than Mr Bush did in 2000 (when John McCain was pretty much it). Her repositioning has already opened up space to her left which is being filled by Russ Feingold and John Edwards. As Ronald Brownstein of the *Los Angeles Times* argues, the former may become the Howard Dean of the 2008 campaign. The senator for Wisconsin has been a consistent critic of both the Iraq war and Mr Bush's war powers; he was the first senator to endorse a time-line for withdrawing and the only one to vote against the Patriot Act in 2001. He has also assiduously cultivated the netroots (he is a regular blogger on the *Daily Kos*). Mr Edwards is developing the theme that he first sounded in 2004—that America is stratifying into a class society—and he has forcefully renounced his vote in favour of the Iraq war.

Mrs Clinton would be able to see off a left-wing revolt if she had the party's right wing to herself. But many moderate Democrats fear she will never be anything other than a liberal in the eyes of Middle America. And some believe they have an ideal mainstream candidate in Mark Warner. Mr Warner was not only a highly successful governor (remember that only one Democrat in the past 100 years has reached the presidency straight from the Senate); he was a highly successful governor of a Republican state. He succeeded in Virginia by persuading rural and small-town southerners to vote for him. And he was so successful that Virginians voted for another Democrat to replace him. Since the Democrats have little chance of winning unless they can break into the “solid South”, this is a résumé to conjure with.

The big naughty dog in the room

The other hidden difference between the Bushes and Clintons is more personal. Mrs Clinton enjoys some of the same dynastic advantages as Mr Bush did—from name recognition (only 1% of Americans claim not to have heard of her) to nostalgia (62% of them have a favourable opinion of Bill Clinton). But she has one big disadvantage. Nobody expected Poppy and Ba to move back into the White House with Dubya. But nobody expects Mr Clinton to stay in Chappaqua. You don't have to be a wild-eyed Clinton-hater to worry about what he will get up to. Will he try to run bits of the government, thereby creating bizarre constitutional issues? Or will the big dog simply pad around the White House wagging his tail with nothing but time on his hands?

It would be foolish to underrate Mrs Clinton. She has oodles of money and star power. She can rely on a legion of earnest middle-aged Democratic women. And she has a well-oiled political machine, which will be fine-tuned during this year's Senate race in New York. But she is no shoo-in for the Democratic nomination. Keep an eye on Messrs Feingold and Edwards. And above all keep an eye on Mr Warner.

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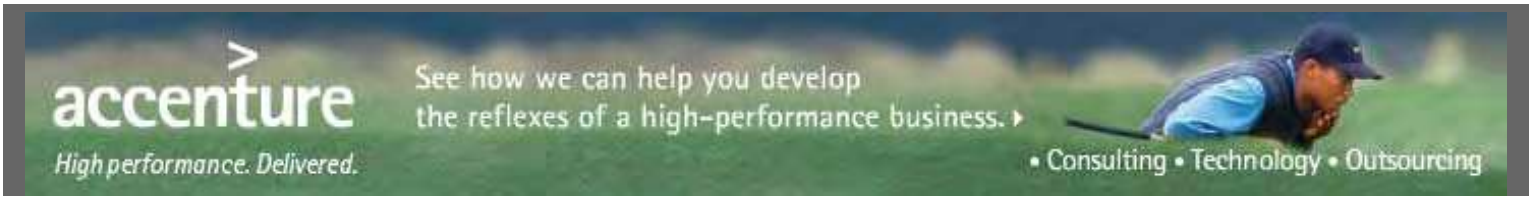
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Mexico and the United States

Shots across the border

Jan 12th 2006 | MEXICO CITY
From The Economist print edition

Plans for a border fence spark anger among Mexicans

Get article background

COUNTRIES that claim to be the best of friends do not normally shoot across their mutual frontier. But on December 30th, an agent of the United States Border Patrol shot dead an 18-year-old Mexican as he tried to cross the border near San Diego. The patrol says the shooting was in self-defence, and that the dead man was a *coyote*, or people-smuggler. Vicente Fox, Mexico's president, made a diplomatic protest, and called for an investigation into the shooting. At the other end of the border, in Texas, Border Patrol agents were reportedly shot at from inside Mexico.

These incidents could hardly have come at a worse time. On December 16th, the United States House of Representatives passed by 239 to 182 votes a bill sponsored by James Sensenbrenner, a Republican from Wisconsin. This would make illegal immigration a felony, create a crime of employing or aiding undocumented migrants, and order “physical infrastructure enhancements” (ie, a fence) along more than a third of the 3,100 kilometre (2,000 mile) border.

The Sensenbrenner bill stands little chance of passing in the Senate. It is not backed by the Bush administration, which has campaigned for tougher enforcement to be combined with a guest-worker programme. This would help give legal status to some of the 10m or so migrants who are in the United States illegally (perhaps 60% of whom are Mexicans).

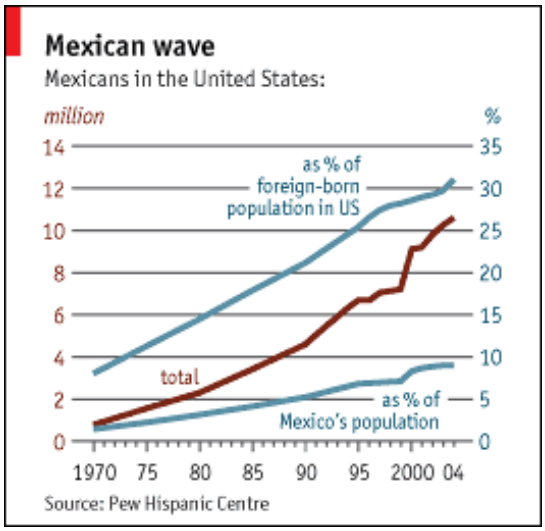
Nevertheless, the Sensenbrenner bill has caused outrage south of the border. Mr Fox called it shameful. He said migrants were “heroes”, who will in any event find ways to cross the border. Luis Derbez, his foreign minister, called the bill “stupid” and “underhand”.

On January 9th, seven Central American countries, together with Colombia and the Dominican Republic, agreed to work with Mexico to defend their emigrants to the United States. Most of these countries have free-trade agreements with America. They are its closest allies in Latin America, where many governments are less friendly than they were a decade ago.

All this is a far cry from the warmth between Mr Fox and George Bush when both took office. Mexico had high hopes of negotiating agreements on migration. Then came September 11th 2001, and Mexico's opposition at the UN Security Council to the war in Iraq. Some Mexicans say the hopes were always unrealistic. Others say that Mexico—and Mr Derbez in particular—must shoulder much of the blame for them being dashed. Mr Derbez threw out a plan for immigration reform drawn up by his predecessor, Jorge Castañeda, largely out of personal animosity. He is widely seen as an unimpressive minister.

Perhaps Mr Fox's biggest mistake has been his failure to lobby effectively over migration on Capitol Hill. Andrés Rozental, who heads the Mexican Council on Foreign Relations (and is Mr Castañeda's half-brother), notes that this contrasts with the effort made to secure passage of the North American Free Trade Agreement (NAFTA) in 1993, when Mexico used its network of over 40 consulates to lobby Congress. Another unused channel of influence is the one-in-12 people born in Mexico who now live in the United States (see chart). Most are there legally and many are eligible to vote.

Despite the public acrimony, Mr Rozental says that day-to-day co-operation between Mexico and the United States on matters such as public health, trade and law enforcement has never been greater. But he believes there is a minimal chance of significant progress on immigration reform under Mr Bush.



There is a broad political consensus that Mexico should push for a guest-worker programme and the regularisation of undocumented migrants in return for beefing up security on its side of the border. None of the candidates in a presidential election due in July is likely to use the issue as justification for anti-American rhetoric of the kind that has become common farther south. Mexico's ties to the United States are too important for that.

But migration will remain a running sore in relations between the two countries. Fences on urban stretches of the border in California and Texas have pushed migrants to the Arizona desert—but have not stopped them. Last year, some 400,000 crossed illegally, of whom over 90% had jobs in Mexico, according to estimates by the Pew Hispanic Centre, a think-tank in Washington, DC. But even unskilled jobs across the border pay much better. NAFTA was supposed to close that gap, but it has not done so yet.

More than 400 Mexicans died in 2005 trying to enter the United States (though in only two cases was the Border Patrol involved). That looms large in Mexican consciousness. Every Mexican knows someone who has crossed the border, if they haven't done so themselves. The harder and more dangerous it gets, the more Mexican public opinion may turn against the United States. The free movement of goods, but not of labour, across the border was always likely to cause problems.

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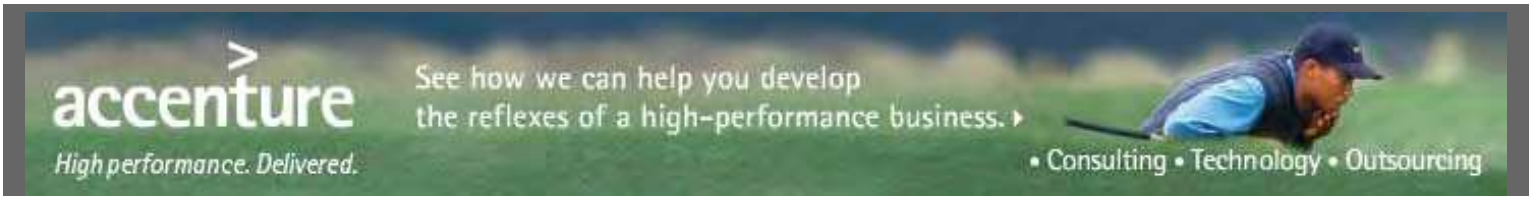
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Chile's presidential election

Belle for Michelle

Jan 12th 2006 | SANTIAGO
From The Economist print edition

The ruling coalition shows its strengths

Get article background

AFP

With a little help from her friends

BARRING last minute surprises, Michelle Bachelet seemed assured of becoming Chile's president in a run-off ballot on January 15th. A poll by MORI this week gave Ms Bachelet 53%, six points ahead of her opponent, Sebastián Piñera, a wealthy businessman and moderate conservative. If that turns out to be right, Ms Bachelet will become only the third woman to be elected president in Latin America. And she will have clinched a fourth term for the centre-left coalition called the Concertación, which has governed Chile with much success since 1990.

Ms Bachelet had long been the favourite. But after several campaign stumbles, she did less well than expected in the election's first round on December 11th. She won 46% of the vote—but that was six points fewer than the Concertación's congressional candidates and three points fewer than the combined vote of Mr Piñera and Joaquín Lavín, the more conservative of the two opposition candidates.

Two things appear to have tipped the contest towards Ms Bachelet, a paediatrician and twice separated mother of three children who was tortured under the dictatorship of General Augusto Pinochet.

The first is that she has closed ranks with the government of Ricardo Lagos, the popular outgoing president. It scheduled debates in Congress on a bill to reform the electoral system, which were calculated to highlight the opposition's internal splits. Ministers have toured the country, inaugurating public works. On January 7th, only hours before Ms Bachelet visited Valparaíso, where she has struggled, Mr Lagos announced a $73m investment in the port city. “We're competing not with Michelle Bachelet, but with a thousand-headed monster—the government,” said an adviser to Mr Piñera.

The second factor is that Mr Piñera will not necessarily secure all of the votes that went to Mr Lavín, who is now nominally his ally. Some of Mr Lavín's poorer supporters mistrust Mr Piñera's wealth. Meanwhile, Mr Piñera's effort to win over centrist voters is not helped by Mr Lavín's past ties to General Pinochet.

Mr Piñera insists that after 16 years of the Concertación, Chile needs a change. But with few big policy disagreements between the two candidates, the Concertación's record—which includes a successful transition to democracy and rapid economic growth—may convince a majority of voters to give it another try.

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Extradition in the Caribbean

Long arm of the law

Jan 12th 2006 | PORT OF SPAIN
From The Economist print edition

No longer such a safe haven for suspected criminals

FOR almost ten years, Noel Heath and Glenroy Matthew, better known as “Zambo” and “Bobo”, have staved off attempts by the United States to extradite them from their homes on the pretty little island of St Kitts to face charges of cocaine trafficking. Their creative legal team has twice taken the case to the Privy Council in London, still the final appeal court for most of Britain's former Caribbean colonies. Both times, most recently last November, a panel of British law lords ruled that they should be extradited “with the utmost expedition”.

“Zambo” and “Bobo” are well-connected in St Kitts. They have lived on bail for a decade, before being locked up last month. Their lawyers hit back with a *habeas corpus* writ, to be heard on January 18th. If that fails, the way is open for officials to put the two on a plane.

For reasons of principle, or of friendships in tight-knit communities, or both, Caribbean countries have been reluctant to extradite their own nationals. The Caribbean has also become something of a haven for foreigners wanted elsewhere in the world. This may now change. The next important test comes in May, when the Privy Council will rule on Samuel “Ninety” Knowles, a Bahamian who has held out since 2000 against an indictment by a grand jury in Florida.

Procedural complexities and powerful lawyers may still stop extraditions. In September in Belize, Dean Barrow, a lawyer who is also the leader of the parliamentary opposition, stymied an American attempt to extradite a drug suspect. He found mistakes in supporting paperwork, which excluded the use of vital wiretap evidence.

Extradition of foreigners, especially to their home country, is often easier. Viktor Kozeny, a Czech-born resident of the Bahamas, has been held in Nassau since October. He is wanted in New York for corruption stemming from the privatisation of Azerbaijan's oil company, and faces other charges in Prague.

Mr Kozeny will fight hard. His lawyers include Philip Davis, a member of parliament for the governing party and former legal partner of the prime minister. Even so, the authorities seem reluctant to grant bail. Perhaps that is because Mr Kozeny holds a pilot's licence and Irish and Venezuelan passports. He was once a diplomat for Grenada.

Non-citizens are sometimes simply expelled. Two Belizean women picked up $50,000 each on the Oprah Winfrey show in October, their reward for spotting an alleged rapist from the United States who was sent home two days later for trial. It is rarely so quick or easy.

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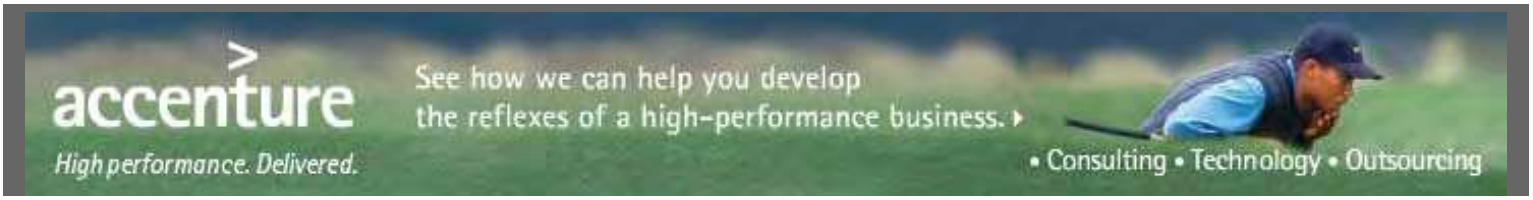
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Venezuela

Slow road ahead

Jan 12th 2006 | CARACAS
From The Economist print edition

A bit more cut off from the world

Get article background

A MERE 16km (ten miles) separates Venezuela's capital, Caracas, from its international airport at Maiquetía on the Caribbean coast. But if they lack a helicopter, travellers might be wise to set off the day before. On January 5th, a viaduct carrying the motorway that crosses the mountains between the capital and the airport was closed indefinitely. Now, the journey can take up to five hours in each direction.

Like much of Venezuela's infrastructure, the viaduct dates from the 1950s. It was built over a geological fault. A mountain has been steadily sliding towards it. Successive governments have known of the problem for 20 years but did nothing. Only when the bridge was on the point of collapse did Hugo Chávez, the president since 1998, tender for a new one, costing $75m. It will not be ready until mid-2007 at the earliest.

For now, the main alternative for the 40,000-50,000 vehicles a day that used the motorway is the old “highway” from Caracas to the port of La Guaira—a twisting, unlit, two-lane road, prone to mudslides. It can take no more than 10,000 vehicles per day. Airlines have been forced to cancel flights, alter schedules and arrange “air-bridges” between Maiquetía and Valencia, two hours west of the capital by road. But that road, too, is in bad shape.

Even worse-hit than travellers are the 300,000 people of the coastal state of Vargas. Many worked in the beachfront tourist trade, which is now paralysed, while thousands commuted to work in the capital.

The motorway was one of Venezuela's most vital arteries, carrying much of the imported consumer goods on which the oil-producing country depends. Shortages and higher freight costs will push up inflation, already 15% but hitherto falling.

The political cost for Mr Chávez, who calls himself a socialist and who faces a presidential election in December, could also be significant. Vargas has been *chavista*. The president's potential challengers trail in the polls. But they have pointed out that he has lavished time and public money on cultivating allies abroad while neglecting crucial infrastructure.

On January 6th, Mr Chávez threatened to nationalise the coffee industry, one of several that has declined to sell goods at controlled prices which producers say are uneconomic. To some Venezuelans, that looked like an attempt to distract attention from the motorway debacle. Mr Chávez champions “endogenous development” for his country. Albeit inadvertently, that is starting to look like autarky.

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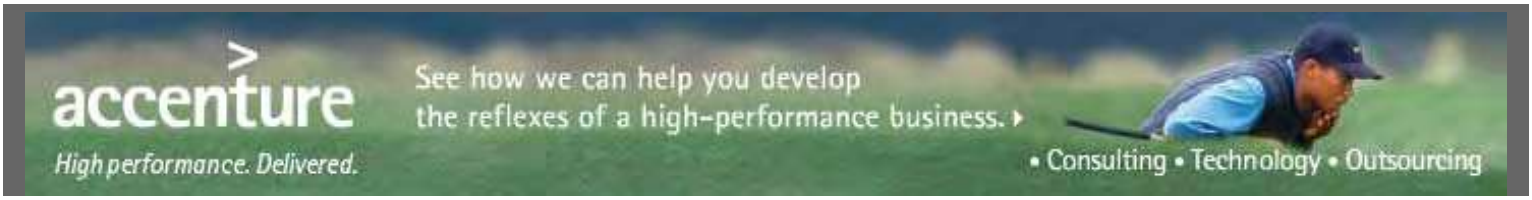
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The media in Argentina

No criticisms please

Jan 12th 2006 | BUENOS AIRES
From The Economist print edition

Caressing and cajoling the messenger

AS HE has done for the past 20 years, Pepe Eliaschev ended his radio show on Argentina's public broadcaster on December 30th by urging his audience to tune in next week. Just minutes later, he says, the station's boss told him that an order had come “from above” to drop the programme, despite a contractual requirement of at least a week's notice.

The sacking of Mr Eliaschev, a critic of the government, is unusual chiefly for its heavy-handedness. Since the return of democracy in Argentina in 1983, freedom of expression has been guaranteed by law. But since then criticism of the government in Argentina's media has never been as scarce as it is now, many journalists say. Through incentives and veiled threats, President Néstor Kirchner has secured a remarkably favourable press.

One of the government's tools is money. The robust recovery in Argentina's economy since its collapse of 2001-02 has boosted tax revenues. That has brought an eightfold increase in the real value of the federal publicity budget (to $46m in 2006) since Mr Kirchner took office in 2003. Argentine governments have a long tradition of funnelling official advertising to sympathetic media and withholding it from others. That applies just as much to provincial governments. According to a study by the Association for Civil Rights (ADC) in Buenos Aires, in the sparsely populated province of Tierra del Fuego official advertising accounts for three-quarters of the total revenues of local media, for example.

The national media are less dependent on public advertising, but have received other favours. The government has been particularly kind to the Clarín Group, Argentina's largest media conglomerate. After the devaluation of the peso in 2002, the group—like many other Argentine companies—defaulted on its dollar debts. When its creditors threatened to take it over, Congress passed a law capping any foreigners' stake in “cultural goods” at 30%. The government has also extended for ten years the group's cable-television licences. Perhaps not surprisingly, Clarín, Argentina's biggest-selling daily has tended to back the government.

Página/12, a left-leaning daily founded to crusade for human rights, was once committed to investigative journalism. It has become a mouthpiece for Mr Kirchner. In return, the government has pumped in money. The ADC reckons that in a sample two-week period in 2004 *Página/12* received just 17% less public advertising than Clarín, although its circulation is small.

Individual journalists have also received official favours. Some of the leading print columnists also rent slots on cable-television channels. They present commentary programmes, receiving some of the ad revenue—much of which may come from the government. “Everyone has mixed interests,” says María O'Donnell, a former correspondent for *La Nación*, the most critical of the dailies. “Journalists are part of the system, and there's no code of ethics to address conflicts.”

Media which have not been co-opted may face low-level coercion. Typically, that means aggressive phone calls from officials after critical stories, followed by the subsequent denial of interviews or seats on the presidential aircraft. Last July, shortly after calling journalists “schizophrenic” and “hysterical”, Mr Kirchner quipped that photographers were the best reporters because they don't ask questions. The president rarely answers them—he has granted no full interviews.

Mainly because of the economy's recovery, Mr Kirchner is popular. He could argue that his predecessors have used many of the same techniques. Carlos Menem used the privatisation of television to secure friendly coverage. An inquisitive photographer was murdered on the orders of a businessman with links to his government. The dictatorship of 1976-83 simply imposed censorship and used violence against journalists.

But there is widespread agreement among journalists that Mr Kirchner has taken government influence over the media to a new peak of subtle intensity. He is taking other steps to concentrate power in his own hands. He has announced a plan to change the independent judicial council to give him more sway over the courts. Argentines may come to rue a lack of scrutiny of their government.

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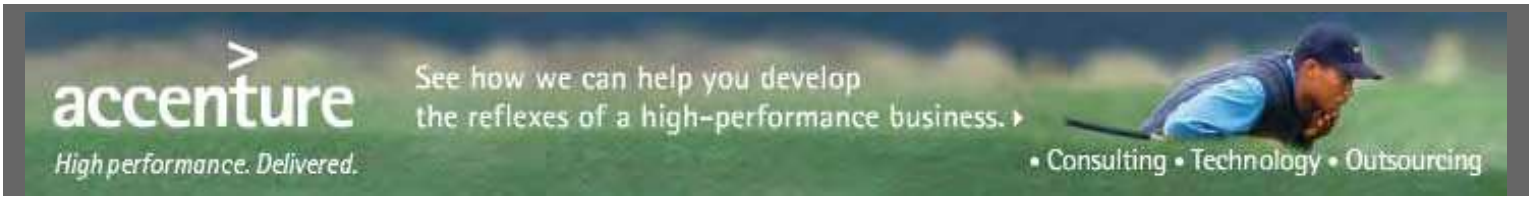
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China

The long march to privacy

Jan 12th 2006 | BEIJING
From The Economist print edition

Gradually, China's people are acquiring the right to be left alone—as long as they keep quiet about politics, of course

IT IS surely telling that the characters that make up *yinsi,* the Chinese word for “privacy”, carry the connotations of illicit secrets and selfish, conspiratorial behaviour. The notion of privacy has not traditionally been valued in China, and proof of that is on display everywhere. The country's public lavatories are often open-plan affairs where locals unabashedly squat elbow-to-elbow as they tend to their business. In hospitals, modesty is often thrown to the wind as treatments are carried out in full view of milling crowds. In the most casual of social interactions, complete strangers think nothing of asking each other details—about their salary, weight and so on—that most westerners would not share even with close friends.

Despite all this, there are signs that the concept of privacy is gaining currency. Echoing the debates now common in western societies, many in China are beginning to bristle at the intrusiveness of nosy employers, data-mining marketers and ubiquitous security cameras.

It is a remarkable development, considering where things stood just a few decades ago. When China's communist rulers came to power in 1949, they set few limits on their freedom to pry into the lives of ordinary people. In the heyday of state control, the Chinese had their employment, housing, health care, food rations and travel all micromanaged by bureaucrats, and their lives were open books. Women of childbearing age even had their menstrual cycles monitored so the state could ensure that those without permission did not get—or remain—pregnant.

The worst of that is now long past. In most respects, people have taken far greater control over their own lives as central planning has begun yielding to the market. Many Orwellian controls remain firmly in place, however, over politics, religion and free expression. Earlier this month, Microsoft acceded to a Chinese request to shut down a blog carried on its MSN service and written by an outspoken government critic, Zhao Jing, who also goes by the pen name An Ti.

In another case, the Chinese government asked for and received from Yahoo!, an internet company, the information it needed to trace the identity of a Chinese internet user, Shi Tao. Mr Shi was arrested in late 2004 and sentenced last April to ten years in prison on charges of revealing secrets by e-mail. Microsoft and Yahoo! have

both reaped withering criticism for co-operating in these cases.

For Chinese citizens, it is clear that privacy rights enjoy only the flimsiest of legal protections. China's constitution, postal law, labour law and medical law all make passing mention of privacy concerns, but they are vaguely worded and are all anyway subject to the notoriously arbitrary workings of the Chinese legal system. Yet some pundits reckon that, as attitudes toward privacy continue to change, the law will eventually be strengthened.

One such is Professor Lu Yaohuai, of China's Central South University. He thinks that earlier attitudes toward privacy were shaped largely by traditional living arrangements whereby families of several generations often lived together in small homes. He notes that the average living space for urban Chinese had risen from 3.6 square metres (39 square feet) in 1978 to 11.4 square metres by 2003, and says this increase has played an important role in fostering expectations of privacy within the family, especially among the younger generation. Parents in the past would readily enter a child's room, or read a child's letters, without asking, says Mr Lu, but today are likely to incur the wrath of their privacy-conscious children if they do. A number of academics are going so far as to call openly for stronger privacy laws.

In the public sphere, it is usually technology, rather than nosy parents, that attracts complaints. Though it still lags behind Britain, which leads the world with its 4.2m surveillance cameras, China is installing them at a steady clip. Shanghai alone has 200,000, and plans to double that number within five years. The city of Guangzhou has budgeted $26m to install security and traffic-monitoring cameras on all its main streets. Perhaps most high-tech of all is Beijing, where road cameras, equipped with night-vision capabilities, are paired with radar guns and can snap the number plates of speeding motorists at any time of day or night. Drivers are then notified of their infractions via text messages sent to their mobile phones.

Increasingly sophisticated marketers are also taking advantage of technology to obtain and exploit information about consumers' credit histories and buying habits. And Chinese employers are checking what employees do on the internet.

Several cases, though, have sparked public debate. In one, students have complained about the security cameras installed in the corridors of the girls' dormitories of Renmin University in Beijing. Though school officials insisted they were there for the safety of the students, the girls were concerned about being watched as they went to the showers.

In another well-publicised case, a Shanghai bank worker complained when she lost her job because her employer monitored the steamy messages she had sent her boyfriend from a company computer. Earlier this month some policemen balked at a perceived invasion of their privacy. In an anti-corruption measure, the city of Nanjing has demanded that police officers notify their superiors whenever they marry, divorce, travel abroad or buy a car or flat. The edict has prompted complaints from legal scholars and some police officers, one of whom told state media that he believed his bosses were “intruding too much into my private life”. How times change.

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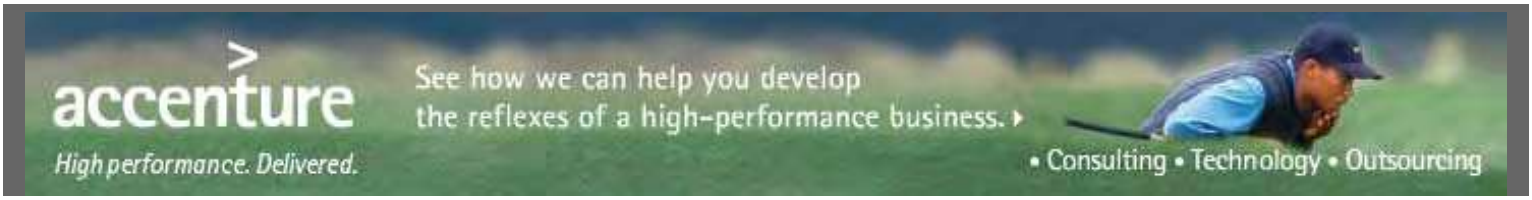
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Asian environmentalism

More hot air

Jan 12th 2006 | BANGKOK
From The Economist print edition

Asia's latest contribution to global warming

Reuters

Gas disgorgers

IT'S catching. David Letterman, an American comedian, joked last year that George Bush would like to respond to global warming by convening “a blue-ribbon committee to explore innovative ways of ignoring the problem”. Now environmental groups are accusing several Asian countries of doing the same thing, in the Asia-Pacific Partnership on Clean Development and Climate. The members of this new outfit—America, Australia, China, India, Japan and South Korea—insist it will complement other efforts to combat global warming, such as the Kyoto Protocol. But critics dismissed the club's first meeting, which ended in Sydney on January 12th, as a fig leaf, a smokescreen and a “coal pact”, among other terms of derision.

Environmentalists would be delighted if they thought the members of the partnership were serious about taking action on climate change. After all, they account for roughly half of the world's population, economic output and greenhouse gases blamed for global warming. They include both the countries with the biggest total emissions (America and China) and the country with the biggest emissions per person (Australia). Moreover, of the six, only Japan is currently trying to cut down its gaseous output in accordance with the Kyoto Protocol, which sets mandatory reductions for rich countries. Both America and Australia refuse to sign the treaty, while China, India and South Korea, as developing countries, are exempt.

But critics claim that the partnership is designed precisely to reduce the pressure on these countries to join whatever pact follows Kyoto, which is due to expire in 2012. They note that, unlike Kyoto, the partnership explicitly rejects mandatory caps or reductions as a useful way to cut emissions. The group's founding charter actually states several times that none of the commitments it contains is legally binding. Instead, the six will simply try to promote greener technology. America and Australia, for example, pledged $128m to fund research in such fields as cleaner coal-burning power stations and safer nuclear plants.

Such technology will certainly be an element of any strategy to reduce greenhouse gases. America, Australia, China and India all have abundant supplies of coal, and rely on it to generate much of their power. For Australia, it is also a valuable export. China and India alone already account for roughly a fifth of the world's greenhouse gases, and their share is growing along with their economies. They are also worried about energy security. Unless some method can be found to reduce the carbon-dioxide emissions from coal-fired power plants, then any successor to Kyoto will be meaningless. No wonder, then, that much was made at the summit of an Australian pilot

project now under way to capture emissions of carbon dioxide (the main greenhouse gas) and store them underground, one version of a process known as sequestration.

It is hard, however, to imagine private firms adopting fancy—and expensive—new techniques without clear financial or regulatory incentives to do so. When questioned about this, Samuel Bodman, America's energy secretary, lamely replied that high-powered executives, like everyone else, have children and grandchildren and so care about the future of the planet.

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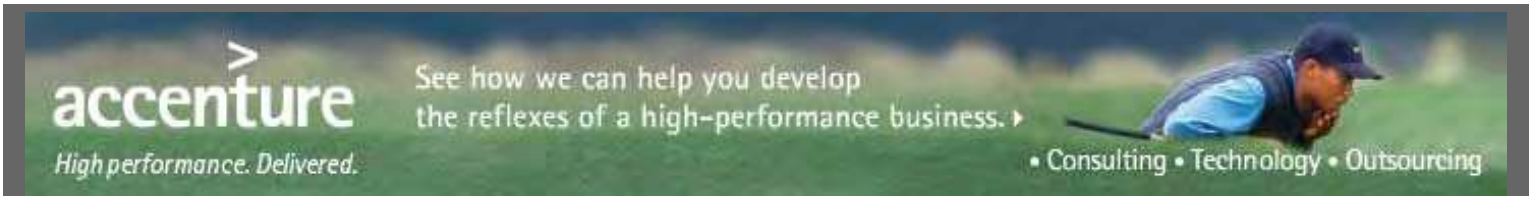
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Economic growth

The jobless boom

Jan 12th 2006 | BANGKOK
From The Economist print edition

A first-world problem is hitting Asia

UNEMPLOYMENT is not normally considered a problem in Asia. Most adults, and quite a few children, are simply too poor not to work. They make whatever living they can, often as subsistence farmers, or, increasingly, as casual labourers in cities. Moreover, Asian economies generate lots of jobs each year, thanks to their tigerish growth.

But many Asian countries, it turns out, are generating job-seekers even faster. The number of the unemployed in the region has risen every year since 1999, albeit from a low base. The International Labour Organisation reckons that some 74m people, or 4.4% of the workforce, are currently out of work across Asia and the Pacific.

Those figures do not include the legions of underemployed. According to a recent report from the Asian Development Bank (ADB), a fifth of the workforce in Pakistan, a quarter in Nepal and over a third in Bangladesh do not have as much work as they want. In Vietnam, the underemployment rate for rural workers is put at 56%.

Demography is exacerbating the trend. Most countries in the region still have relatively youthful populations, so more people enter the job market each year than leave it. The ADB predicts that China's workforce will grow by 7% by 2015, Indonesia's by 14%, Pakistan's by 30% and Afghanistan's by 43%. If more women start working, as they are doing throughout the region, the growth in the labour pool will be even more dramatic.

Young Asians are already struggling to find jobs. Those between the ages of 15 and 24 make up a fifth of the workforce, but half the unemployed. In Sri Lanka, younger workers are six times more likely to be unemployed than older ones.

Asia's growth, in other words, is simply not creating enough jobs: and not only is the ratio of employment growth to economic growth low, but it also appears to be falling pretty much across the board (see chart). This may seem odd. In countries where labour is cheap, growth should be more labour-intensive than capital-intensive. But in Asia, argue Jesus Felipe and Rana Hassan, the authors of the ADB's report, modern, export-oriented firms, which have underpinned much of the recent growth, are likely to use the same technology as their first-world counterparts. That may explain why, in 2000, the number of jobs created in China for each unit of economic growth was less than a quarter of what it was in 1990. Only subsistence farming and simple urban services are highly labour-intensive, and these are not thriving industries. Asia, welcome to the jobless boom.

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Sri Lanka

Truce and fiction

Jan 12th 2006 | COLOMBO
From The Economist print edition

How many violations make a war?

Get article background

IT IS beginning to look less like a ceasefire, and more like an undeclared war. Early on January 7th a vessel laden with explosives detached itself from a flotilla of fishing boats off Trincomalee in north-eastern Sri Lanka. Its suicidal crew steered it into a Sri Lankan navy fast-patrol craft. Two sailors saw it coming, jumped and were later fished from the sea. Thirteen of their shipmates died, bringing to more than 50 the number of military personnel killed since the beginning of December. Then, on January 12th, at least nine sailors died when a bus they were travelling on was blown up by a mine. The presumed attackers, the Liberation Tigers of Tamil Eelam, who have fought for a Tamil homeland for two decades, deny involvement. Nobody believes them, and a Tiger-affiliated website has linked the ship attack to the killing, blamed on the Sri Lankan army, on January 2nd, of five Tamil students. The Tigers say thousands of people are taking refuge in their territory, having fled government-controlled areas in the north where the army is cracking down brutally on suspected Tiger sympathisers.

Both sides, in other words, are trying to make the other look the belligerent party. Neither wants the blame for bringing a formal end to the four-year-old ceasefire. But a group of monitors, under Norwegian leadership, says the truce is facing its most serious crisis yet. This follows the election in November to the Sri Lankan presidency of Mahinda Rajapakse, portrayed by the Tigers as a diehard chauvinist from Sri Lanka's Sinhalese majority.

Yet, by enforcing an election boycott in their areas, it was the Tigers who in fact helped bring about Mr Rajapakse's victory. As Velupillai Prabhakaran, the Tigers' ruthless leader, made clear in his annual “heroes' day” speech just after the election, the Tigers had never put any faith in the peace process. Rather, they “wanted to demonstrate beyond doubts that the Sinhalese racist ruling elites would not...offer a reasonable political solution.”

The attacks since the election seem part of a strategy to provoke the government into the kind of harsh retaliation that will lose it support abroad. In their statements, Mr Rajapakse and his colleagues are refusing to read from this script, preaching moderation and insisting they want a negotiated settlement and renewed talks with the Tigers. On the ground, however, a demoralised, besieged army seems less restrained. And the government's quibbling over where the talks should be held, rejecting the Tigers' suggestion of Oslo, makes it seem less wholehearted in its commitment to peace. Like the Tigers, though, it wants foreign approval and money—which is why, for now, full-scale war seems as unlikely as real peace.

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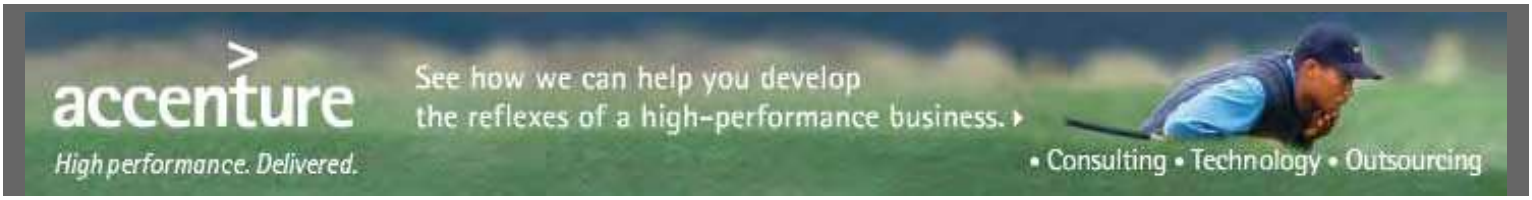
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Myanmar

Busy, busy, busy

Jan 12th 2006 | BANGKOK
From The Economist print edition

The UN's man quits in disgust

AP

Get article background

The unseen Razali

THE generals who run Myanmar are busy men. So busy, in fact, that for the past two years they have not found any time to squeeze in a visit from Razali Ismail, the UN official charged with restarting the country's transition to democracy. On January 8th, Mr Razali announced his resignation.

Mr Razali is not the only man the generals are refusing to receive. The UN's human-rights monitor for Myanmar, Sergio Pinheiro, has not set foot in the country since 2003. Even the junta's supposed friends in the Association of South-East Asian Nations (ASEAN) have been cold-shouldered of late. At the group's annual summit last month, Myanmar's prime minister agreed to receive a delegation to be led by Malaysia, currently in the chair at ASEAN, early this year. But now the time has come, he and the rest of the top brass find themselves run off their feet.

The failure to accommodate either Mr Razali or ASEAN seems particularly bad news, in that both were thought to have won the junta's trust. It was Mr Razali who in 2002 brokered the release from house arrest of Aung San Suu Kyi, Myanmar's Nobel-prize-winning democracy advocate, only to see the generals confine her again the following year. ASEAN, meanwhile, admitted Myanmar in 1997, on the theory that engagement would yield better results than ostracism. Yet the junta now seems as indifferent to ASEAN's overtures as it is to criticism from America and the EU.

Mr Razali speculated this week that the Security Council would eventually take up the subject of Myanmar if the junta did not appear to be co-operating with anybody else. The council did hold an informal debate on Myanmar late last year. But it seems unlikely that China, which relies on Myanmar both for energy supplies and a military base on the Indian Ocean, will allow any serious criticism of the junta. Even if it did, the generals would probably pay no attention. They are, after all, already too busy ignoring everyone else.

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India

Thundering herds

Jan 12th 2006 | SONITPUR DISTRICT, ASSAM
From The Economist print edition

The battle to conserve India's elephants

THERE are, by one count, 58 insurgent groups in the seven states that make up India's north-east, a region of bewildering ethnic diversity. In recent months, in the Karbi Anglong district of Assam state, more than 100 people have been killed in clashes between ethnic Karbis and Dimasas. But Assam is also home to glorious biodiversity. Tigers, rhinos and elephants still roam the forests. They too are victims of the insurgencies, and wage their own conflicts with their human neighbours.

In Sonitpur, a district on the North Bank of the Brahmaputra river, the war between people and elephants has claimed nearly 150 human and 80 elephant lives since 1996. About 2,000 elephants live in the area. But their homelands in the thickly wooded Himalayan foothills, despite being legally protected as reserved forests or wildlife sanctuaries, have been invaded by poachers, timber thieves and settlers. Short of the food they need to sustain their mighty frames, elephants have taken to snacking in the paddy-fields, villages and tea plantations of the valleys.

Moving along time-worn paths, the huge creatures, often so gentle and amiable, are a fearful menace to the humans in their path, and to crops and livelihoods. At the Tarajulie tea estate, Ravinder Singh, the manager, says the elephants started visiting five or six years ago, coming just after the October-November rice harvest. Now they come throughout the year. A herd of 37, browsing peacefully in a bit of jungle at the edge of the estate one recent afternoon, look harmless enough. But at 2am one night last September, close to the nearby village of Ranganijar, several elephants overran one little farmhouse. Cyril Tanwar, a 45-year-old man, sleeping with his young son, was crushed to death. “We're not harming them, why should they harm us?” asks his sister-in-law.

To help answer that question, local activists, helped by WWF, an international conservation group, have been proselytising on the elephants' behalf. They have created, for example, an educational puppet show, illustrating, among other horrors, the dangers of distilling alcohol when there are elephants about: they are boozers as well as gourmands. In fact, most locals do not need persuading that the root of the problem is human encroachment rather than elephant greed. Elephants are still widely worshipped in the form of the god Ganesha. Near Ranganijar, a little temple was erected to Ganesha, over the grave of a small calf that died in an irrigation culvert in a tea estate. The god was not appeased: elephants destroyed it.

Elephant protection is hazardous. Fifty “anti-depredation squads”, each of a dozen local villagers willing to spend their nights on elephant watch, have been equipped with firecrackers and searchlights and trained in steering hungry herds from fields, homes and stills. Some are helped by *kunkis*, trained, domesticated elephants. Three such—two adults and a calf—went into battle at Tarajulie. The mahout riding the lead elephant, armed with a shotgun, was fuelled with local firewater. Local lads joined in the fun, releasing deafening firecrackers. After one false start, the herd emerged from the trees. One rogue, an elephant from another herd in “must”, ie, on heat, who had already had his way with one of the herd, stayed behind, to terrorise the tea-workers. The others fled single-file, lolloping across a river back to their familiar forests.

Elephants can be deterred by electric fences, where they can be afforded, or, it is hoped, by a rope smeared with a pungent mixture of grease and hot chilli peppers. This technique—a success in Africa—has been imported by WWF. Even obedient *kunkis* refuse orders to breach the eye-stinging ropes. An experimental fence is guarding a field of sugar cane, which elephants like as much as alcohol.

Conservationists, however, know that all of this is a sticking-plaster, not a cure. In

the long run, only afforestation can save the elephants. By the WWF's estimate, 29% of the lowland forest in Sonitpur was lost or degraded between 1991 and 2001. Workers at a local air-force base are unabashed when caught removing firewood from “fallen trees” (with suspiciously clean stumps) in a protected patch of forest.

The elephants' twilight

Illegal settlers, similarly, seem unconcerned about their future, fencing off land they have cleared. Some have been evicted in the past, and simply moved back. In this region, most are Bodos, a people for whom insurgents have been fighting for an independent homeland, though a ceasefire is now in place. Analysts believe the encroachments were part of a planned expansion of settlements to lay claim to such a homeland, though Sonitpur is not in fact part of the Bodoland Territorial Autonomous District, declared in 2003.

It seems too much to hope that the Bodos will move to their designated district. Nor does the government show much sign of enforcing its laws. The money allocated in Delhi for far-off Sonitpur seems to get lost in transit. But without more concerted action, the war between elephants and humans can only worsen. And, watching the despondent line of harried elephants from Tarajulie, heading off at dusk to forage for food in their depleted forest, it is easy to guess who will be the losers.

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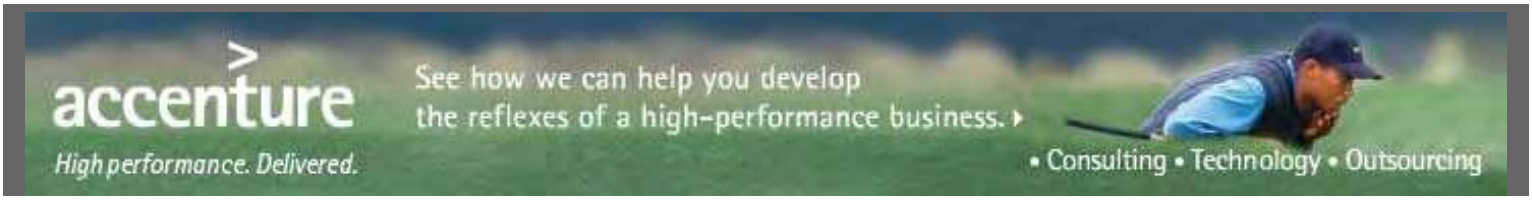
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Israel

Searching for the middle ground

Jan 12th 2006 | JERUSALEM
From The Economist print edition

Why voters supported Ariel Sharon, and why, even as he remains critically ill, they might still support his party

Get article background

OBESE, waddling, pompously leaden of rhetoric, with a war record that some consider criminal and a squint that broadened with every passing year: outsiders never found it easy to comprehend what Israelis saw in Ariel Sharon. But since last week's brain haemorrhage, which has locked his plans for the future into unreachable recesses of his mind, another riddle has arisen: did those who saw something in the prime minister see anything else besides? Did the polls that put his new centrist party, Kadima ("Forward"), streets ahead of its rivals, Labour and the Likud, reflect merely a blind faith in Mr Sharon's abilities to do the right thing, and will those voters now drift back to their old parties? Or is there a new Israeli "centre" that Kadima can appeal to—and if so, what does it believe in?

After an early wobble, Kadima is rallying around Ehud Olmert, the acting prime minister. Shimon Peres, the veteran Labour leader who joined it, has been persuaded to stay in. Mr Olmert, a seasoned politician, looks set to lead it to the election on March 28th. A poll this week suggests that Kadima under Mr Olmert may win 44 of parliament's 120 seats, two more than the last poll under Mr Sharon.

That, however, may be a temporary sympathy vote. And, as Kadima's rivals are quick to say, there are plenty of grounds for scepticism. Mr Sharon created Kadima not as a political concept but merely as an escape vehicle from hardline rebels who were undermining him in the Likud, points out Yuri Shtern, a legislator from the right-wing National Unity party, which represents Russian-speakers. Ephraim Sneh, a Labour security hawk, snipes that Kadima is not a centre party but "Likud Lite", led mostly by Likud moderates who jumped ship with Mr Sharon. Chaim Oron of the left-wing Meretz suggests, rather, that Kadima's members' views are so broadly spread that they will have trouble cohering on their own. "They trusted Sharon precisely because he didn't say exactly where he was going; they were willing to go along with him but not take part in a decision in advance."

Such trust was due to Mr Sharon's mythical status. What made him credible, if not actually lovable, to mainstream Israeli Jews was that he reconciled their belief in the need to give up occupied territory with their deep suspicion of the Palestinians since the violent collapse of the Oslo peace process in 2000. They felt that, as a father of the settlement movement, he would give up settlements, as in Gaza, only when truly necessary, and in a unilateral process that Israel could control.

In fact, Mr Sharon embodied two deep-rooted aspects of the Israeli psyche, argues Moshe Naim, editor of *Kaan Naim*, a paper aimed at the country's geographic and political centre. He would let no one—least of all "the Arabs"—take him for a *fraier*, a sucker, the greatest indignity an Israeli can suffer. And he had the earthiness of the *amkha*, the mythical Israeli common man. Labour and Likud both have prominent representatives of the *amkha*, says Mr Naim, "but in Kadima there is an uncomfortable sense of snobbism"—personified best by the cigar-smoking Mr Olmert.

Looked at this way, Kadima's prospects look slim. Previous centrist parties have fizzled. To top it all, Mr Sharon left behind no future plan—at least not a public one—which Kadima could call its own.

Yet polls suggest that there is a centre there for the taking. Roughly two-thirds of Jewish Israelis want a Palestinian state, says Ephraim Yaar, a co-author of Tel Aviv University's monthly Peace Index poll, but about the same number believe that the Palestinians "would destroy Israel if they could". Former rightists, like Mr Sharon, have rejected the right's insistence on keeping all of "Greater Israel", including the occupied West Bank; old leftists have lost trust in the left, not for its ideas but "for the faith it put in the Palestinians". The result: a large block which believes in territorial separation, but on Israel's terms. Israelis want an end to Palestinian violence first, says Eyal Arad, an adviser to Mr Sharon, and Palestinian independence only afterwards. The 21st-century Israeli: not an expansionist, but not a *fraier* either.

Kadima, says Otniel Schneller, a former settler leader who recently joined the party, will aim for the mid-points on the three main axes of Israeli opinion: land versus peace, welfare economics versus the free market, and the level of religious influence on civil affairs. Previous centre parties, he says, have usually taken the extreme position on at least one of these, or have focused on domestic matters, while Kadima will put national security, voters' top priority, first.

It helps Kadima that both Labour and the Likud have moved towards the fringes. The Likud lost its moderates to Kadima. And its leader, Binyamin Netanyahu, who pushed through needed but unpopular economic reforms during a stint as finance minister, has even more of an elitist image than Mr Olmert. At the other extreme, Labour's new leader, Amir Peretz, a trade-union man, is as *amkha* as it gets, but hurt himself early on with rash promises about a quick peace deal. Both men, says Mr Yaar, have fixed themselves in the public perception: it will be hard for them to win back moderates who backed Mr Sharon.

So Kadima could coast through the election to lead a coalition with Labour—unless an explosion of Palestinian violence fortifies the right. But if the test does not come before the election, it will come afterwards. With the Palestinian Authority's grip on power weakening and Hamas, the Islamist opposition, set to do well in elections in the West Bank and Gaza this month, there may soon be nobody that Israel will agree to hold peace talks with.

The big unknown is what Mr Sharon would have done then. Many assume he would have eventually started dismantling West Bank settlements unilaterally too. But Mr Yaar's polls show that only a small fraction of Israelis currently favour unilateral steps, even if the alternative is to put the peace process on ice. If opinion changes, as it could, the first question is whether Kadima can agree on a policy. And the second is whether Mr Olmert, though he proposed unilateral disengagement publicly before even Mr Sharon did, would have the credibility to force it through. For now, though, none of his immediate rivals has any more.

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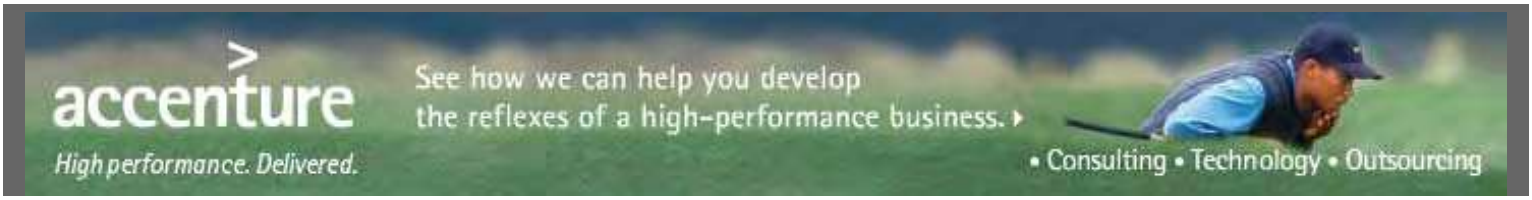
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Egypt

New dawn or more of the same?

Jan 12th 2006 | CAIRO
From The Economist print edition

Egyptian politics still looks grubby, yet the mood has shifted

AFP

Same old pharaoh

AN ODD text message popped up on Egyptian mobile phones in the last days of 2005. “The price of an *ulla* leaps to $10,” it said. An *ulla* is not some hot stock on the Cairo exchange. It is a cheap clay jug which, by Egyptian custom, you smash on the threshold of your house when an unwanted guest leaves, to make sure they never come back. The purported scarcity of *ullas* was due, as any clever person would infer, to the end-of-year cabinet reshuffle that saw the abrupt departure of several long-serving but widely loathed ministers. Yet in many Egyptian minds, the desire for door-slamming riddance might apply to the year as a whole.

Apart from the Cairo stock exchange, whose index rose 125%, 2005 was sadly inglorious. The improving picture for the country's economy made little difference to families struggling as ever with poverty, unemployment and diminishing public services. Presidential and parliamentary elections, heralded as the freest in decades, turned out nearly as fraudulent as usual, returning the same president of the past 25 years, Hosni Mubarak, at the head of the same ruling party. Talk of greater human rights was belied in practice by numerous graphic incidents of police excess, most shockingly by the busting on December 30th of a sit-in by Sudanese refugees that saw at least 27 people, including infants and grandparents, crushed or beaten to death by Cairo's riot squad.

The other images of the year that linger are of a terrorist attack that killed 88 people at the resort town of Sharm el-Sheikh; of plain-clothes government thugs groping women protesters in a Cairo march; of voters scaling ladders to reach polling stations during November's parliamentary elections, after police had blocked the doors to opposition supporters; and of the candidate who was runner-up in the presidential contest, Ayman Nour, being put behind bars for five years on a flimsy forgery charge that many Egyptians interpret as punishment for daring to present a liberal alternative to 77-year-old President Mubarak, who is now set to rule until 2011.

Yet if Egypt looks very much the same top-heavy, police-ridden state as it has since the 1952 coup that ushered in what some describe as a presidential monarchy, much has changed below the surface. The most populous (70m-strong) Arab country, and in many ways the most influential, is clearly in a phase of transition, though no one seems to know towards what.

The clearest portent for some is the dramatic advance of the Muslim Brotherhood. Though officially banned, Egypt's oldest Islamist group won most of the parliamentary seats it contested in November. Probably fearing an Algerian-style government response should they have done too well, the Brotherhood fielded candidates for just 141 out of 444 seats, yet it emerged, with 88 MPs, as the biggest opposition block to sit in an Egyptian parliament since the last king's removal.

Such electoral success was partly a reward for the Brotherhood's formidably efficient organisation, as well as for its adoption of a more inclusive message that stresses democratic freedoms rather than enforced Islamisation. But it also reflected widespread public anger with the regime, as well as the state's diminished capacity to control the press, trade unions and other public forums. The Brotherhood may have captured the same kind of popular will for change that has fostered secular movements in such places as Serbia and Ukraine. The ruling National Democratic Party's candidates lost two-thirds of the races they ran in, despite widespread rigging. The party kept its traditional rubber-stamp majority by coaxing scores of “independent” winning candidates to join, largely in the hope of getting more perks for themselves and constituents.

How to hold on

Mr Mubarak's party, still firmly in charge, has a two-pronged strategy to stay in power. The Brotherhood's success lets the NDP pose as the only alternative to Islamist rule, a stance that appeals to Egypt's worried Christian minority as well as to secular Muslims, many businessmen and also, presumably, many western allies. Mr Nour's imprisonment and the government's unwillingness to license a long-proposed centrist Islamist party hint that the regime actually wants to keep Egyptian politics polarised.

The other prong is economic. Egypt has pursued liberalising reforms since the 1970s, but the government's commitment has often wavered, due to concerns, for example, that privatisation of state assets would weaken the government's power to coerce workers or supply cosy sinecures to loyal officers. That hesitancy has lessened: witness the naming of a new cabinet dominated by prominent businessmen rather than party stalwarts or ex-army men. With Egyptian coffers filling nicely from gas exports, record Suez Canal tolls and booming tourism, the bet is that economic growth will remain a buffer against social upheaval. Maybe. But then some revolutions—in Iran or France, for instance—came along just when middle-class expectations were rising.

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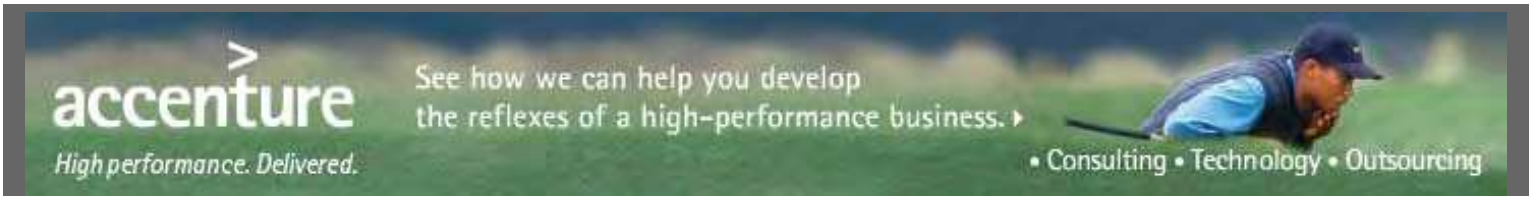
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South Africa

Spend more but wisely

Jan 12th 2006
From The Economist print edition

The climate for investment is sunny, so why isn't more being invested?

Get article background

LAUNCHING his ruling African National Congress's campaign for local elections due in March, President Thabo Mbeki recently promised that his government would splash out more than 400 billion rand ($66.4 billion) on infrastructure over the next five years: hardly a surprising pledge, since the government has secured low inflation (3.7% at present) and a healthy budget, and has already started to loosen the purse strings. Mr Mbeki's main aim is to expand the economy by more than 6% a year (the latest rate is 4.2%), above all in the hope of cutting South Africa's miserable unemployment rate, which is officially around 26% but may really be as high as 40%. Yet public and private investment has been stuck at a disappointing 15-16% of GDP for the past five years, about half the level of Asia's bounciest economies. Why so sluggish?

In a study out last month, the World Bank and South Africa's trade and industry department asked 800 private South African companies about the investment climate. The answers they gave are encouraging. When compared not only to African countries but also to places like Malaysia, Brazil and eastern Europe, South Africa looks good. Most firms say that local courts work well; property rights are adequately protected. Power is comparatively cheap, tax rates fairly low. Red tape is no worse than in other countries with similar per capita incomes.

Perhaps more surprisingly, labour productivity is higher than in Brazil, Poland, Malaysia and even China. This is because South African firms, by comparison, rely more on capital than labour. In addition, most South African firms surveyed find it easier to borrow. In any case, they do not have to call the bank that often—on average they are more profitable than their counterparts in, say, Poland or Malaysia—so they have more spare cash to invest.

So what are South African companies grumpy about? About a third of firms surveyed complain about labour regulations. An earlier World Bank report showed that, though South Africa is less entangled in red tape than many other countries, its companies find it harder to hire and fire. And most companies that export have been worried by South Africa's previously wobbly exchange rate. The rand underwent several crises in the 1990s; its value against the dollar has more than doubled since 2001. Crime is another pain. About a third of South African businesses say they are hampered by it. Security and crime-related losses cost them about 1% of sales, higher than in Russia or Brazil. Yet they do not have to pay protection money, as many firms in eastern Europe and Asia do.

Even in such problem areas, things are looking up. Crime is down. The exchange rate is steadier. Investment and growth are both improving. But the worst drawback for South African business is its scarcity of skills, something that cannot be altered fast. South African firms offer far less training than their competitors in China, Poland or Brazil. Labour costs are more than three-and-a-half times higher than in the most productive areas of China and a good 75% higher than in Malaysia or Poland. The gap is especially wide for highly qualified workers. Salaries for unskilled ones are roughly the same in South Africa and Poland, but South African managers earn over twice as much as Polish ones. An extra year at school in South Africa brings a salary increase of 11-12%, whereas workers in developed countries can expect to make only 5-7% more.

This skills shortage has slowed down public investment too. With government finances now in order, the problem is not money but the ability to spend it. Many municipalities underspend their investment budget because they have too few qualified people to design and manage projects. Now that the government is willing to spend more, it is unclear how fast—and how well—the huge dollops promised by Mr Mbeki can actually be invested.

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Uganda

All the presidents' wives

Jan 12th 2006 | RUHAMA COUNTY
From The Economist print edition

It helps to have a well-known husband in the forthcoming elections

AFP

The first lady makes a fist of it

WITH its rolling green hills, thin trees and friendly people, Ruhama, in south-western Uganda, might just be God's country. Come Sunday, the churches are packed with believers praising the Lord in prayer and song. No surprise, then, that Uganda's first lady, Janet Museveni, an evangelical Christian born here in 1949, chose this constituency to run for a parliamentary seat in next month's elections. God has sent her to do this, she says, so she must obey.

Her minders from the ruling National Resistance Movement, the party run by her husband, President Yoweri Museveni, get a bit twitchy when asked about Mrs Museveni's rapturous talk. They explain that her would-be constituents implored her to stand, and she prayed before accepting. Opposition groups, however, offer their own gospel. Her decision, they say, had rather more to do with her cousin, a local district chairman of the ruling party, than with God.

Whatever the truth, Mrs Museveni, who argues for abstinence as the main way to stop the HIV infection, will not be the only woman with connections to the president's office spicing up the poll. In the presidential race, Mr Museveni, running for a third time after MPs tamely altered the constitution to let him have a third term, has a clear lead over his nearest rival, Kizza Besigye. But they are both being challenged by Miria Obote, widow of the late president, Milton Obote. She is standing for his old party, the Uganda People's Congress, which ran the country from 1962 to 1971, and again from 1980 to 1985, before Mr Obote was chased out of Uganda after a coup by Mr Museveni.

Clearly not to be outdone, Mr Besigye's wife, a former opposition MP, has re-emerged as a political force too. On his return from self-imposed exile last year, Mr Besigye was swiftly arrested on charges of treason, terrorism and rape, but is now out campaigning, on bail. His wife, Winnie Byanyima, once a close friend of Mr Museveni, has put herself at the centre of the electoral fray by alleging that two judges took bribes from military intelligence to put off her husband's release from prison.

Liberia recently made history by electing Africa's first female head of state, Ellen Johnson-Sirleaf. Uganda will not make that sort of stride yet; Miria Obote is unlikely to win. But Mrs Museveni could make an impact. She and her husband operate separate networks within the inner circle of western Ugandans who run the country; at first, Mr Museveni even opposed his wife's wish to stand for parliament at all. But she is pretty sure to win a seat, and should have a strong mandate in her own right.

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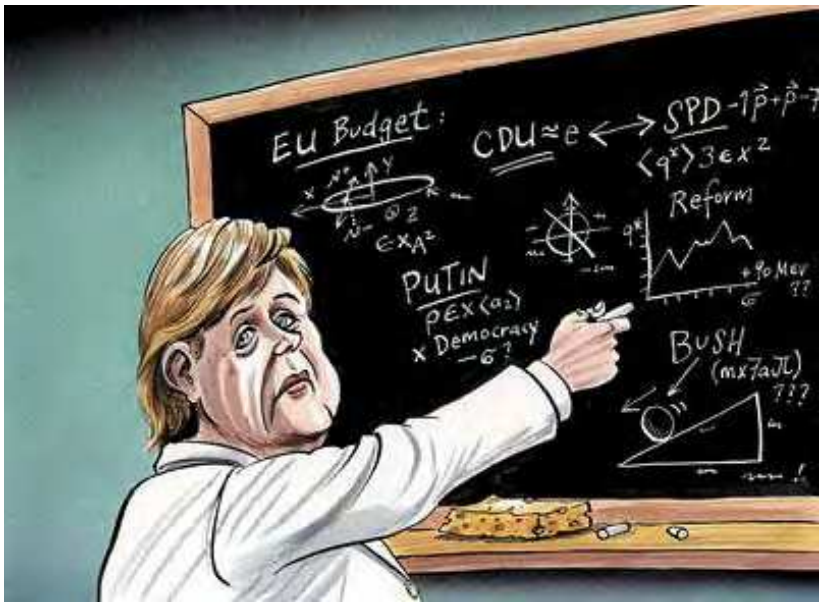
Germany's government

The Merkel method

Jan 12th 2006 | BERLIN
From The Economist print edition

Ahead of Angela Merkel's visits to America and Russia, there is much interest in her views—and her methods



IS SHE up to the job? During the election campaign last summer, her political foes tried their hardest to spread doubts about whether Angela Merkel had the right stuff to be chancellor. Now, even before her first 100 days are up, it is safe to say that she has: few government leaders have had such a smooth start, and some 60% of Germans think she is doing a good job. That is not a bad platform from which to start her first tour beyond Europe, which will take her this week to Washington and Moscow.

A much harder question is whether her government will prove to have the right stuff to tackle Germany's intractable problems. In the months to come, Ms Merkel's grand coalition of her Christian Democrats with the Social Democrats will be put to the test. This week's cabinet retreat marked the end of the honeymoon between the two parties that began when the coalition was formed in November.

Already the press is talking of a “Merkel method”, particularly evident in foreign policy. Many decisions by Gerhard Schröder, her Social Democrat predecessor, seemed to come straight from the gut, but Ms Merkel's appear to be born at the back of her brain. Rather than charging ahead, she carefully analyses a situation and then takes pragmatic, problem-solving action. It is as if this doctor of physics sees political configurations as a science experiment, in which she lets different forces play out before intervening.

This approach has served her well to overcome her party rivals. Instead of fighting with them directly, she let them tire each other out and ended up on top. Ms Merkel seems to have done something similar at the European Union summit in December, when she coaxed France's Jacques Chirac and Britain's Tony Blair into a budget deal. Of course, it helped that she also revived another German tradition of writing a big cheque, even finding some extra cash for Poland at the last minute.

This is not the only reason why some foreign-policy analysts talk of the second coming of Helmut Kohl, a former chancellor and Ms Merkel's mentor. In her tour of Europe before Christmas, she manoeuvred Germany back into the position of the EU's “honest broker”. Yes, the Franco-German friendship is crucial, was the message in Paris,

but it should not be too close for comfort. Yes, she said in London, my economic thinking is more British than Mr Schröder's, but Germany will not ditch its social-market economy. When Germany takes over the EU presidency in early 2007, she hopes to find some way of reviving the EU's moribund constitution.

In transatlantic relations, Ms Merkel is demonstrating that she knows all about force and counterforce. With her pro-American credentials not in doubt, she can be more candid than Mr Schröder, who won re-election in 2002 by openly opposing the war in Iraq. This week she said that “an institution like Guantánamo Bay in its present form cannot and must not exist in the long term.” Yet such statements contain nothing aggressive, argues Ulrike Guérot, of the German Marshall Fund; rather, they are the basis of a revitalised relationship. Her visit to George Bush is mainly intended to get to know each other, though she may also announce an increase in non-military aid to Iraq. (This week it also emerged that German spies in Baghdad had helped the Americans pick bomb targets during the war in Iraq.)

Ms Merkel's trip to Russia is likely to bring further careful corrections. She will give Vladimir Putin a harder time than Mr Schröder ever did. Western concepts of democracy cannot just be schematically grafted on to Moscow, she recently said, but added “I do admit that I'm concerned about some recent developments, such as the new laws against NGOs.” On the vexed issue of Iran, Franz-Walter Steinmeier, her new foreign minister, has set the pace. By breaking the UN seals on its nuclear installations, Mr Steinmeier said this week, Iran “has crossed a line which the Iranians knew would not remain without consequences”. This must put in doubt any further negotiations between Iran and the EU three of Britain, France and Germany.

Domestically, it is too early to know if the Merkel method will work. Since last September's election, which she saw as a rejection of rapid reforms, she has often sounded almost like a Social Democrat. But she also has a multi-stage plan to give Germans back their “belief that politics matter”, in her own words. The first stage is to boost the country's morale, which she is trying to do in speeches. “I want to encourage you to find out what you are capable of. I am convinced you will be surprised,” she said in her new-year address.

The second stage is to help the economy with spending measures worth €25 billion ($30 billion) over the next four years, whose details were announced this week. This hotch-potch of measures will try to push up demand this year, while still making it possible to keep the promise to cut the budget deficit below the EU's stability-pact ceiling of 3% of GDP in 2007.

So far, at least, the economy seems to be perking up, though one would be hard-pressed to attribute this in any way to actions by the new government. The general mood has improved and most economists have raised their growth estimates for 2006 to as much as 2%. The big risk is that the value-added tax increase planned for 2007 could nip the incipient recovery in the bud. And the longer-term question is whether the third stage of Ms Merkel's plan will ever happen: getting her grand coalition to agree on reforms to meet the country's structural problems.

Although there are many reforms on the government's to-do list, such as measures to help the long-term unemployed and energy policy, the one to watch is health-care finance. The Christian Democrats want a new flat-rate insurance premium, decoupling health-care contributions from salaries. But the Social Democrats want to keep the link to pay, and to find other forms of income, such as capital gains, as a new financing source.

If Ms Merkel can broker an intelligent compromise on health care, other reforms, such as an overhaul of the tax system, or of the equally messy federal system, may start to look possible. Only then will the “Merkel method”, which is now best known as a way of modelling heat exchangers, come to stand for cool, level-headed politics as well.

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A Frenchwoman in politics

The Ségolène effect

Jan 12th 2006 | PARIS
From The Economist print edition

A popular female politician whom the Socialist Party refuses to take seriously

AFP

A Royal flush

ONE by one, they filed past to pay their respects. Last weekend, a parade of Socialist grandees gathered at the Jarnac cemetery to remember François Mitterrand on the tenth anniversary of the former president's death. With one notable absentee: Ségolène Royal. While the Socialist bosses marked the past, the darling of the French left jetted off to meet the future: a trip to Chile to back Michelle Bachelet, its (female) Socialist presidential candidate (see article).

Ms Royal's media-savvy foreign excursion comes at an awkward time for her party's leadership. For months, as her poll ratings have climbed, Socialist heavyweights have queued up to dismiss the president of the Poitou-Charentes region as a media mirage. But the more they write her off, the more her popularity grows. In one poll for *Le Figaro*, she beat not only Bernard Kouchner, the ever-popular humanitarian doctor, but even Nicolas Sarkozy, the centre-right favourite and head of the ruling UMP party. As a presidential candidate for the left, two other new polls put her firmly as top choice.

Surely the party should be pleased to have such a popular favourite ahead of next year's presidential election? It is due in November to select its candidate, and there is no clear front-runner. Moreover, the Socialists are still smarting from divisions caused by the decision of Laurent Fabius to lead a rebel camp against the European Union constitution. This week, Mr Fabius, a former prime minister, said he would run for the party's nomination, adding haughtily, apropos of Ms Royal, that “all poll predictions have always been wrong.” Dominique Strauss-Kahn, a former finance minister, is expected to declare soon too.

These internal rivalries may make it harder to unify behind a single name. Hence the persistent chorus talking Ms Royal down. “She has no foreign or economic experience, and a very difficult personality,” sniffs one insider. There is also the small complication that her partner is the Socialist Party's boss, François Hollande. Could he sink his ambitions to promote hers? Could they somehow run as a double ticket?

Perhaps the most intriguing endorsement of Ms Royal has come from Mr Sarkozy, not usually one to praise the left. She is, he says, “the most interesting” Socialist personality. They resemble each other, he adds, as “atypical” politicians. In one sense, he has a point: each has cultivated an image as an antidote to the Parisian elite, an outsider in touch with ordinary folk. But in another, his motive is less flattering. The more she is promoted as a serious contender, the more divided her party will be—and the better the prospects for Mr Sarkozy.

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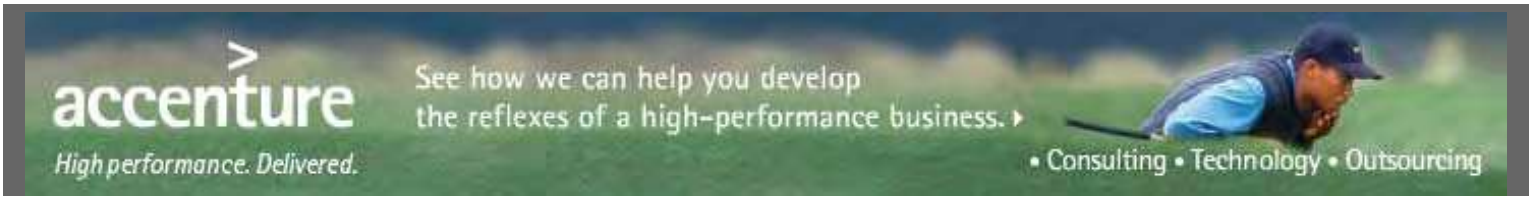
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Spain and Catalonia

Bad echoes from the past

Jan 12th 2006 | MADRID
From The Economist print edition

An errant general tests the prime minister's talent for compromise

SPARE a thought for Spain's satirists. How can they match the decision by the defence minister, José Bono, to order eight days' house arrest for the head of the land forces, General José Mena Aguado? The general, who was due to retire in March, had publicly exhorted his fellow officers to defend Spain's unity against the prospect of a law giving more autonomy to Catalonia. He spoke of a "deep disquiet" over the planned statute, which acknowledges Catalonia as a nation, replaces Madrid's constitutional court with the regional high court as Catalonia's highest judicial authority, gives it broader tax-raising powers and obliges officials to speak Catalan. "The armed forces have as their mission to guarantee the sovereignty and independence of Spain," trumpeted the general.

Mr Bono will now ask the cabinet to sack him. One irony is that his comments were in the tradition of burlesque patriotism that Mr Bono himself so often displays. Yet the general struck a nerve in a country that has seen dozens of military coups over the past 200 years. The civil war of 1936-39 that led to Franco's dictatorship began partly because the army took exception to Catalan autonomy. Democracy was restored only in 1975; another comic-opera coup was tried six years later.

This incident has ratcheted up the row over Catalonia's new statute, and increased tensions between the Socialist government of José Luis Rodríguez Zapatero and the opposition. Spain's political agenda is now dominated by the issue. Mr Zapatero, whose minority Socialist government relies on Catalan nationalist votes, has left himself open to the criticism that he is a lightweight who has let his tenure be taken over by regional squabbling.

Last November the Cortes, Spain's parliament, voted 197-146 to accept the Catalan statute and send it to its constitutional committee. The opposition People's Party (PP), which says the plan is unconstitutional, voted no and has tried to block its progress. A PP spokesman said that General Mena's latest *pronunciamentito* was inevitable in the prevailing climate. The PP leader, Mariano Rajoy, argues that "the whole Catalan statute is built on a false assumption that Catalonia is a nation, so it is sovereign...and has a right to decide by itself its relations with the Spanish state."

The Catalan dispute is being watched closely in the Basque country, the other region that always wants more autonomy. It has also encouraged less restive places. Socialist-ruled Andalusia is toying with a definition of itself as a "nation". One wag suggested that such a putative al-Andalus might see Osama bin Laden as its spiritual father. A similar reform in the PP-governed Valencia provoked less reaction.

Mr Zapatero has declared that the Catalan statute is unacceptable in its present form. But he seems to have persuaded most Spaniards that the PP is scaremongering. "When the Catalan statute is approved and in force, I will remind you [ie, the PP] that you were wrong and deceived the citizens, because nothing is at risk," he said. In keeping with his instinct for compromise, Mr Zapatero has told Catalans that the statute heralds a new dawn, yet at the same time assured Spaniards that nothing of substance will change. But the conservative newspaper *ABC* noted that the statute deepens "the abyss between the two visions of Spain held by Zapatero and Rajoy," and also pointed to its "elastic, imprecise and ambiguous" language.

The final version of the statute is likely to be substantially altered; more than 500 amendments have been proposed. Even many Socialists have threatened to oppose it unless it is watered down. The toughest wrangling is over how much tax autonomy to cede to Catalonia (Socialist-run Extremadura and Andalusia are both anxious to keep fiscal transfers from Spain's richest region) and the use of the word "nation". The Catalans want to keep 90% of their income taxes; Madrid may offer a compromise of 50%. Mr Zapatero has also suggested "national identity" as a better phrase than "nation". Yet striking a deal on either point will be hard.

Despite the fuss on the centre-right and in the army, most Spaniards seem not to care much. Opinion polls still

give the Socialists an edge over the PP, although the lead is shrinking. At the start of his tenure Spain's prime minister remarked that it was easy to govern Spain because he had “demystified power”. That claim might hold good so long as he can keep telling everybody what they want to hear and amiably fudging through. But a fudge may not prove possible over Catalonia.

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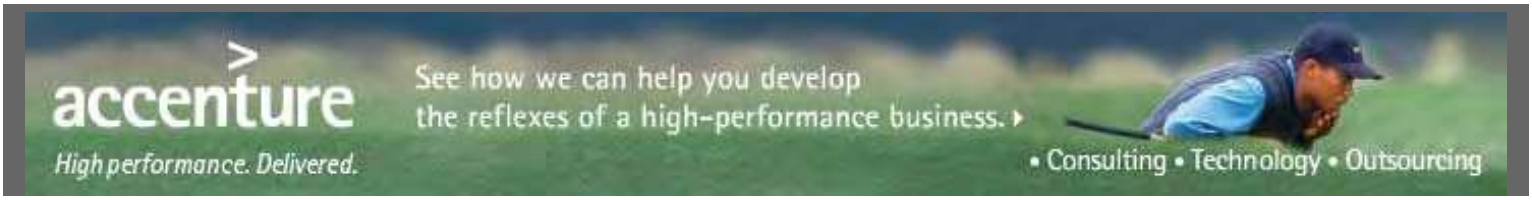
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Turkey and bird flu

When the chickens come home to roost

Jan 12th 2006 | ANKARA
From The Economist print edition

The despair, and the hope, surrounding Turkey's bird-flu outbreak

Reuters

WAS it yet another conspiracy to sabotage Turkey? That was one explanation dished up by some in Recep Tayyip Erdogan's ruling Justice and Development Party for the outbreak of bird flu across the country. By mid-week, at least 15 people in Turkey had been diagnosed with the deadly H5N1 strain of the disease, and three children had died—though only two were confirmed cases. The deaths of the siblings, in Dogubeyazit, near the Iranian border, were the first bird-flu fatalities outside South-East Asia, where some 76 people have died of the disease since 2003.

Panicked Turks have been flooding hospitals with complaints ranging from tummy-aches to high temperatures. In Ankara, three people have already tested positive for H5N1. All had been in contact with sick animals. In Istanbul, with a population of 10m, three neighbourhoods with infected poultry were put in quarantine. Over a quarter of Turkey's 81 provinces are reported to have infected birds.

Turkey is the first country to report so many separate animal cases simultaneously. This, plus an unusual cluster of mild human cases in Ankara, may give some cause for hope. Perhaps the disease is less virulent than was first thought; in Asia many mild cases may have gone undetected since only those with serious symptoms tend to go to hospital. More worrying is the possibility that, since some of the Ankara cases had only limited contact with birds, the disease may have changed in ways that makes it more easily transmitted from birds to humans.

A ban on Turkish poultry imports had already been imposed by the European Union. Domestic sales of poultry products have plummeted by 90%. Because Turkey is a transit route for migratory birds from the Balkans, Siberia and the Black Sea, further outbreaks seem inevitable. Worst of all may be the impact on Turkey's tourist industry, a mainstay of the economy.

One other plus is that the World Health Organisation declared this week that the Turkish government had performed satisfactorily, at least in dealing with the human cases. “The action in the country has been appropriate and the management of this crisis is at the level where it should be,” commented Marc Danzon, the WHO's regional director. Yet this sanguine view is not shared by many Turks, who accuse the government of a cover-up. When Mehmet Ali Kocyigit, a 14-year-old, died on January 1st, Turkish health officials said at first that the cause was pneumonia. Cemil Cicek, the justice minister, accused health officials who had raised the alarm over bird flu of “mischievous behaviour”. It was not until late last week, just before the second Kocyigit child died, that the health minister, Recep Akdag, confirmed that her brother had contracted bird flu.

Mr Erdogan insisted this week, after over 300,000 birds had been culled, that the situation was fully under control. But his words were contradicted by television footage of children frolicking with chickens in the east. In fairness, the challenge facing the government is huge. Heavy snows and rugged mountains have prevented health workers from reaching many villages thought to have infected birds. And many Kurdish villagers do not understand Turkish, the only language used in many warnings about bird flu.

But the biggest obstacle is the poverty that propels millions of families to breed backyard poultry. The practice leaves the animals vulnerable to infection from migratory birds. Many families are known to be concealing some or all of their birds. In Erzurum, one citizen offered to turn in his two wives rather than his chickens. The government has yet to come up with a satisfactory compensation scheme. Worse still, local mayors, particularly in Kurdish areas, have proved inept at dealing with the outbreak. In Dogubeyazit, municipal workers even told children to help them catch birds with their bare hands.

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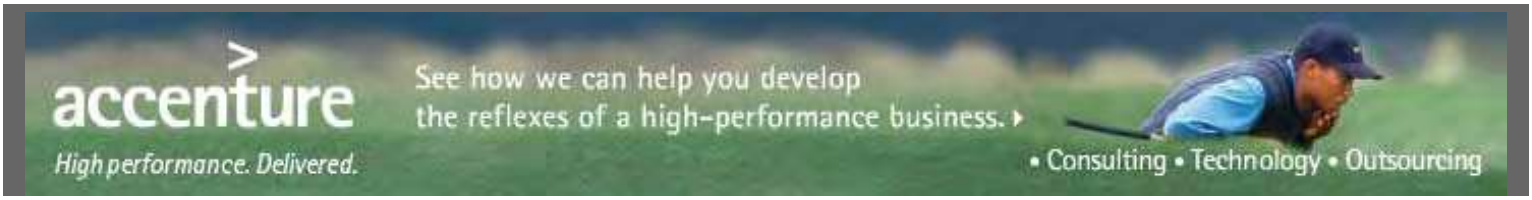
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Poland's shaky government

New ideas

Jan 12th 2006
From The Economist print edition

A promising new finance minister, but plenty of problems lie ahead

TO ITS critics, Poland's right-wing minority government was doomed even before it took office in October. It depends on the votes of cranky populist parties; it is short of talent; and it is run by the slightly weird Kaczynski brothers (Lech is president of Poland; his identical twin, Jaroslaw, leads the ruling Law and Justice party). Its provincial outlook seemed likely to cripple Poland on the world stage.

The new government has shown a weakness for populist gimmicks: the justice minister intervened to free a bunch of vigilantes who beat a petty criminal to death; a deputy prime minister said that doctors who did not co-operate with health reforms should be drafted into the army. But the Kaczynski twins and their prime minister, Kazimierz Marcinkiewicz, are proving wily operators. Mr Marcinkiewicz negotiated effectively at the European summit last month. Poland is taking command of NATO forces in Afghanistan in 2007, while also maintaining troops in Iraq.

At home, the government has wrongfooted its main opposition, Civic Platform, by appointing as finance minister one of that party's brightest former stars, Zyta Gilowska. Her predecessor, Teresa Lubinska, was wildly out of her depth in the post, as shown both by some bizarre public statements denouncing foreign investors and praising budget deficits and by her inept management of the ministry. Ms Gilowska secured a deputy prime ministership to give her added clout. Her appointment has sent the zloty soaring.

What is good for the government is bad for Civic Platform. Its leadership had sidelined Ms Gilowska, ostensibly on charges of nepotism, after she gave a job to her son. Many thought that the real reason was that she was an outsider, a brainbox with a provincial background, not a member of the charmed circle of reformers in Warsaw. Now others from Civic Platform's ragged ranks may follow her. There is a tempting vacancy as privatisation minister, after Andrzej Mikosz resigned last week over criticism of a loan his wife once made to a controversial businessman.

Ms Gilowska's appointment has annoyed the populist parties on which the government depends for support. Self Defence, a leftish outfit led by the demagogic Andrzej Lepper, said the government was “exposing its liberal mask”; the League of Polish Families, a right-wing party with an anti-Semitic youth wing, called it an “appalling error”. But they will still back the government in the forthcoming budget vote: the parties' poor poll ratings make early elections a threatening prospect.

There is plenty for Ms Gilowska to do. Making the public finances more transparent would cut waste and corruption. The tax bureaucracy wastes much of the time of Polish firms. But questions remain over the government's economic policy. Can Ms Gilowska, who lacks a power base of her own, fight off spending ministries? Can she make good on her enthusiasm for a 15% flat tax, a policy that Law and Justice dismisses as unfair? And when will Poland join the euro? The government may have disarmed its domestic critics, but it has some tough decisions ahead.

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CLASSIC
PERTH 2006

Ukraine's government

Pipe down

Jan 12th 2006
From The Economist print edition

The explosive political fall-out from the Russian-Ukrainian gas deal

AFP

Pressure points

IS A bad deal worse than no deal at all? That is the question facing Ukraine, which last week won a six-month reprieve on Russia's plans to quadruple the price of the gas it supplies. Yet opposition parliamentarians, led by a fiery ex-prime minister, Yulia Timoshenko, say that the deal, which will raise the price of gas from $50 per 1,000 cubic metres to $95, is still too expensive. This week they peremptorily voted to dismiss the entire government.

That sounds like a dramatic setback. Since the 2004 “orange revolution”, the pro-western government of President Viktor Yushchenko has been losing credibility both at home and abroad. Russian influence, which crashed after the Kremlin clumsily backed a rigged presidential vote in November 2004, has been returning. The row over gas was a sharp reminder of Ukraine's continued dependence on the goodwill of the country's northern neighbour.

But the government is not dead yet. The legal status of the parliamentary vote is unclear. Mr Yushchenko, who this week called the decision “incomprehensible, illogical, and wrong”, plans to challenge it in court. Most observers expect the government to last until the next election, which was anyway due in March. It is unlikely that any political group will have an overall majority after the election. Ukrainian politics will continue to be a story of horsetrading, in which big business, and Russian money, will play a role.

Perhaps the hardest question for a new government will be whether Ukraine can diversify its sources of energy. The new deal with Russia foresees extra deliveries from gas-rich Central Asia—but through Russian pipes, and handled by Rosukrenergo, a murky intermediary company of the kind much favoured by Russia's gas tsars. It might make sense to back a new gas pipeline from Central Asia across the Caucasus that would be independent of Russia. But such action would require a strong, far-sighted government, of which there seems little prospect as yet.

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Charlemagne

Third time lucky?

Jan 12th 2006
From The Economist print edition

The European Union has stumbled twice in the Balkans. Now it has a chance to make amends

EVEN as European Union leaders yammer about resurrecting their constitution, their attention this year may end up focusing instead on the Balkans. Twice in the past 15 years, the region has tested the EU's claims to have ended wars on the continent: in 1991-92, when EU members split over backing independence for Slovenia, Croatia and Bosnia, and in 1998 when they stood by as Serbs and Albanians slaughtered each other in Kosovo. Now three events are coming together to turn the first half of 2006 into a third chance for the EU—and perhaps the trickiest period in the Balkans for some years.

The first is a referendum on independence in Montenegro. If passed, it would take yet another slice off Serbia (with which Montenegro exists in uneasy union). Next, talks on the independence of Kosovo (also nominally part of Serbia) could result in an offer of conditional independence, meaning that the rights of the Serb minority in Kosovo are protected by international guarantee. And third, the European Commission will rule in May on whether Romania and Bulgaria have met the conditions for EU membership. Had this ruling been made last year, say commission officials, the answer would have been no. That would make headlines, even if its effects prove less obviously dramatic than the break-up of the former Yugoslavia. (If the ruling is no, the two countries will merely join in 2008, instead of 2007.)

What the three events have in common is that they will change the Balkans' fragile status quo (with luck for the better, but it would be foolish to count on that). All are also reminders of the importance of the EU's role. Only Brussels can promise local politicians that their future lies in integration with Europe, not with their historical grievances and inward-looking nationalism. EU countries have promised to help Montenegro if it plumps for independence. And although Kosovo's future is being hammered out under the auspices of the United Nations, it will in practice be the EU that will have to look after the place.

On the face of it, the Europeans have been making good on past promises of help. Last year saw a flurry of negotiations in which nearly every Balkan country started some form of talks with Brussels. Croatia began full membership talks in October (at the same time as Turkey). Bosnia and Serbia began the preliminary stage that should lead to talks. In December, the EU gave Macedonia formal status as a candidate (a step up from Serbia and Bosnia, a step below Croatia). Talks to get Albania to the preliminary stage continue. And three economic deals have been done between the Balkans and the EU.

Yet even all these may add up to no more than a good start. Ultimately, the EU's powers of persuasion rest on the lure of full membership. Now the onset of “enlargement fatigue” risks undermining that promise. Recently, the disease has broken out even in that bulwark of expansion, the European Commission. One commissioner has said that the EU should let in Romania and Bulgaria, but then close its doors. Enlargement fatigue may not only reduce the EU's appeal. It could also make it harder to dole out interim benefits that go with membership talks, such as aid for new roads or help with agricultural reform. Last month's budget deal has already cut the money earmarked for Balkan reconstruction by about a fifth.

The Balkans will anyway not respond to the EU's gravitational pull in the same way as did the central and eastern Europeans. The Balkan people are further removed than the Czechs and Poles were from EU standards of democracy and free markets. They have to set up functioning governments before they can become functioning democracies. This means that much of the Balkans will have to wait for membership even longer than did the central and eastern Europeans. And it is no longer clear how long accession can retain its allure, or how attractive the “pre-accession” phase can be made.

At worst, there is a risk that the EU could end up dividing the Balkans, rather than modernising it—splitting the region into countries on the road to membership (Bulgaria, Romania, Croatia, Macedonia) and the ghetto of the rest, whose status would be uncertain and whose “pre-accession” limbo might be made worse by cuts in aid. For Bosnians and Serbs, there is a danger of EU membership becoming like an old Soviet joke: we pretend to prepare for membership, they pretend to be ready to give it to us.

The virtues of Austro-Hungarian imperialism

Doubts over the EU's influence in the Balkans will be either allayed or confirmed over the next six months. At minimum, it must avoid the divisions and passivity that bedevilled previous episodes in ex-Yugoslavia. But it could do better. And by happy accident, the EU presidency—usually a silly arrangement for each country to set the agenda for six months—has fallen at this critical juncture to the largest single investor in the Balkans and one of the strongest supporters of EU membership for Balkan countries: Austria. The Austrians may be notoriously hostile to Turkey's membership aspirations, but they have said that the Balkans are their top foreign-policy priority. What is less clear is whether they are ready to spend political capital to get reluctant partners to do things to give the rhetoric substance.

Michael Emerson of the Centre for European Policy Studies, a think-tank in Brussels, suggests that Balkan countries might be given membership of the customs union between the EU and Turkey, replacing a tangle of 31 regional trade agreements. He also proposes that the EU should encourage Balkan countries to set up visa-free travel among themselves, to avert travel restrictions that would otherwise arise as some countries join. These are good ideas in themselves, but more important is the message they would send: that the Balkans matter even when blood is not being shed, and that the EU wants to improve the entire region, not just (to borrow a phrase from the constitutional debate) to cherry-pick the bits it likes best.

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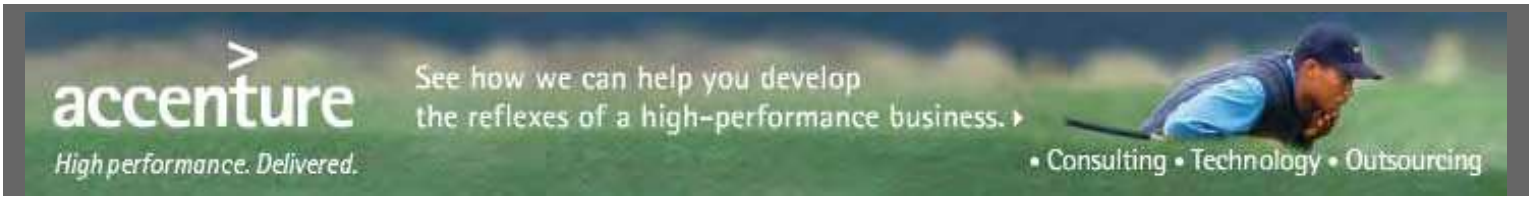
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Anti-social behaviour

Soothing the savage breast

Jan 12th 2006
From The Economist print edition

Tough rhetoric aside, Britain's war on incivility is entering a surprisingly conciliatory phase

Get article background

TONY BLAIR is back in the bully pulpit. On January 10th, he declared that he was jettisoning centuries of legal precedent. He lambasted the criminal justice system, which, he said, protects the accused better than their victims. Then he quietly unveiled a plan to tackle petty criminality and anti-social behaviour that was startling for its moderation, at least by comparison with what has come before.

Britons may not suffer more from incivilities such as graffiti, spitting and verbal abuse than other nations, but they certainly make more of a fuss about them. MPs hear so many complaints from their constituents that Tony Banks, a former left-wing MP who died on January 8th, described one legislative attempt to tackle the problem as a "letting-off-steam bill". Since coming to power in 1997, the Labour government has honed weapons against anti-social behaviour that are unmatched for severity in the western world.

The most potent of these is the Anti-Social Behaviour Order (ASBO). This can be handed out for conduct that causes, or even contributes to a general sense of, "harassment, alarm or distress". On the slenderest evidence (including hearsay), perpetrators as young as ten years old can be banned from entering an area, wearing particular clothing or even speaking certain words. Breach the terms of the order, and the maximum sentence is five years in prison. Some 6,500 ASBOs have been imposed since they became available in 1999.

They are enormously popular, as are other powers, such as curfews and "dispersal orders", which can be used to break up groups. MORI, a pollster, found last year that ASBOs were opposed by just 4% of people. The government is confident that Liberal Democrat and Conservative MPs, who oppose the new measures (the Tories almost to the point of sounding like hand-wringing liberals) are on the wrong side of public opinion.

This week's plans would not, in truth, greatly strengthen powers against anti-social behaviour. That would scarcely be possible, given the fierceness of the current laws. "Short of bringing back the stocks, there's not much more we could do," says Les Carter of Leeds City Council.

The toughest-seeming of the powers announced this week (and the one that attracted most media coverage) would allow the police to evict disorderly households from their homes. It is unlikely that such a power would be used often. The law would be hedged with safeguards and restrictions: it is almost impossible deliberately to make children homeless, for example. Besides, any family thrown out of its home would be likely to turn up at a nearby housing office, demanding accommodation—and would often be given it. Local authorities, which work closely with the police, may not be keen on that.

Quietly, almost stealthily, the government's action plan ushers in more sympathetic tools for dealing with misbehaviour. The government plans to set up a parenting academy where social workers and other professionals can learn how to instruct others in the arts of child-rearing. Parents will be invited (or, if their children are really troublesome, ordered) to attend classes. In extreme cases, households will be removed to flats where the children will be fed nutritious food.

Such methods are already being tested in some unlikely places. No British city took a harder line on anti-social behaviour than Manchester, which, by the end of 2004, had dished out four-and-a-half times as many ASBOs per head as London. But Eddy Newman, a Manchester city councillor, says the enforcement drive has reached a plateau. The city is now going in for more touchy-feely stuff—mediation between neighbours, intensive support for troubled youths and leaflets encouraging parents to read to their children at night.

Similar initiatives are under way in Camden, a London borough notorious for tough policies. Camden now has five “youth-inclusion support panels” which try to quell anti-social tendencies before they reach the point where tougher measures are required. It used ASBOs more sparingly last year than in the previous 12 months. That may be the beginning of a trend. The English courts doled out ten fewer ASBOs in the second quarter of 2005 (the most recent period for which figures are available) than they did in the first. It was the first decline yet recorded.

Why the reluctance to use such a powerful and popular weapon? Partly because ASBOs have proved unwieldy. Leeds got the courts to hand out 66 in a single purge, but, according to Mr Carter, would not do so again. Blanket use meant less stigma for the recipients. And ASBOs are not cheap: the council had to defend one in court, at a cost of some £25,000 ($44,000). When granting orders against children, the courts increasingly tack on training programmes, which must also be paid for.

A more serious problem is that tough measures do not appear to placate the public. The British Crime Survey shows that worry about loitering teenagers, noisy neighbours and drunken louts—the sort of menaces the laws are designed to tackle—has barely abated in the past five years. Last year, anxiety actually increased.

It is not that the war on incivility has fallen flat, say those who led the campaigns in the cities. In the most troubled places, tough measures helped to restore order. But levels of tolerance changed, too. Once word got out that the police and local authorities had a powerful new weapon for dealing with annoyances, people began to spot more problems in their neighbourhoods that they wanted sorted out.

Mark Harris, of Leeds City Council, compares the campaign against anti-social behaviour with the birth of the National Health Service in the 1940s. The architects of the NHS assumed that demand would die down after lingering ailments were cleared up. Instead, public expectations simply increased. So it has proved with the war on incivility. As Neil Pilkington, the principal solicitor of Salford City Council, puts it: “The more you do, the more people develop high expectations of you, and the more they complain.”

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George Galloway

Big Blatherer

Jan 12th 2006
From The Economist print edition

His constituents are getting restive

PA

Big Brother is watching you

SINCE George Galloway's election last year as MP for Bethnal Green and Bow—on a stridently anti-war platform that appealed to the many Muslims in his inner London constituency—he has rarely been far from the public eye. His reputation spread to America after a grandstanding appearance last May in front of American senators investigating allegations that he had profited from illegal Iraqi oil sales.

Yet Mr Galloway's most eyebrow-raising escapade to date is his decision, revealed last week, to take part in the fourth series of "Celebrity Big Brother", a reality-TV show in which semi-famous contestants are confined to a house for 23 days. There they argue, drink and flirt with each other, and try to avoid being voted out by viewers. His participation was justified, he said, because some of the money raised from those who vote would go to a Palestinian charity, and the exposure would bring his politics to a wider audience.

Sadly, discussion among his fellow contestants—who include a topless model, a transvestite singer and a woman famous for sleeping with the England football coach—has so far focused on the gynaecological rather than the geopolitical (his supporters accuse Channel 4 of censorship). Mr Galloway was so taken aback by the constant sex talk that he admitted to wondering whether he is as in touch with public sentiment as he thought.

Similar doubts plague his constituents, though for slightly different reasons. Muhammad Abdul Bari, the chairman of a large mosque in Mr Galloway's constituency, remarked to the *Times* that many Muslims see the programme as "indecent". Protestors marched outside Mr Galloway's most recent weekly constituency meeting (held in his absence) demanding that he get back to work.

Indeed, Mr Galloway's public appearances seem to have come at the expense of his parliamentary duties. According to the Public Whip, a website that tracks voting records, he ranks in the bottom 3% of all MPs when it comes to attending votes, one place ahead of Tony Blair. Others ranking lower include the Speaker and Deputy Speakers, who cannot vote, five Sinn Fein MPs, who refuse to attend on ideological grounds, and Rachel Squire, who died last week after a long battle with cancer.

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Politics

Under new management

Jan 12th 2006
From The Economist print edition

The Lib Dem leadership race poses a threat to the party

THE Liberal Democrats have a distinguished genealogy, stretching back to the aristocratic Whigs who drove King George III crazy at the end of the 18th century. For much of the party's modern history, though, it has fought against irrelevance. Then, in last year's election, the Lib Dems had their best result since 1923, attracting more than a fifth of all votes cast, a score that translated into 62 of 646 MPs.

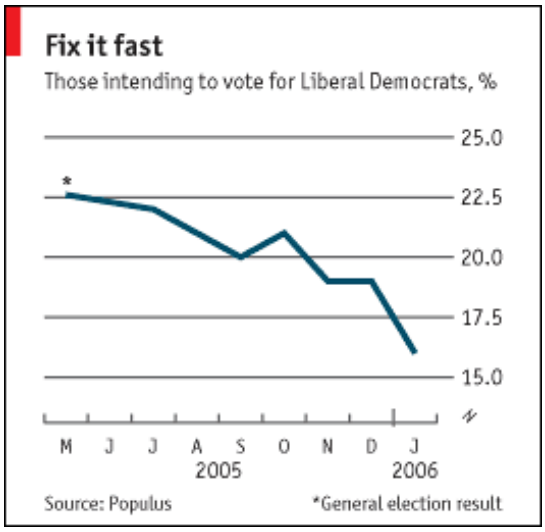
It was a mark of the progress the party had made that many regarded this result, in a fight against two unpopular main parties, as a bit disappointing. Even so, if Labour's fortunes decline and those of the Conservatives rise, the Lib Dems could be left holding the balance of power in a hung parliament. That makes the party's search for a replacement for Charles Kennedy—who resigned on January 7th, two days after admitting he was an alcoholic—more than a mere sideshow, as the vans with satellite dishes parked outside the party's headquarters throughout this week attest.

The leader the party chooses will determine whether the Lib Dems stake out a claim to the increasingly crowded political centre ground, towards which David Cameron is steering the Conservatives, or to territory to the left of Labour (see article). For many Lib Dems, the choice is not obvious; but it is urgent. The party has lost a quarter of its support since last May (see chart), and if it gets its next leader wrong, it could revert to being a charming diversion from mainstream politics.

Three candidates quickly emerged, and a fourth is joining them. Sir Menzies Campbell, a 64-year-old Scottish lawyer and former champion sprinter who was Mr Kennedy's deputy, is the favourite. Sir Menzies is probably the party's best-known figure nationally; as spokesman on foreign affairs he argued against the Iraq war, a stand unique to the Lib Dems among big parties and an important reason for their recent electoral success.

Next comes Simon Hughes, the party's president, a failed candidate for mayor of London who can often be seen driving around his constituency in an old cab. Mr Hughes is on the left of the party and is popular with activists. Mark Oaten, the spokesman on home affairs, is the youngest of the lot and rates his talents rather more highly than his colleagues do. Finally, Chris Huhne, a former journalist (including, in the late 1970s, on *The Economist*) intends to run on a platform including a tougher line on

the environment and a sharper focus on local accountability.



The timing of the election is unlucky for Mr Huhne and other recent arrivals in Parliament. Among them is Nick Clegg, a reformer who has decided it is too early to run himself and so backs Sir Menzies.

Each candidate may spend just £15,000 ($26,525) to woo the single transferable votes of the party's 70,000 members. Under this system, voters rank candidates in order of preference. Votes for trailing candidates are then re-allocated according to second preferences until a winner emerges with 50% of the vote, in time (Lib Dems hope) to hand them victories in May's local elections. A less optimistic reading is that the party will then discover the true cost of keeping a lacklustre leader in place for so long.

For the party's problems did not begin with Mr Kennedy's admission that he had a drink problem. A sense of drift became acute after the general election last May. With the Tories in the midst of a protracted leadership struggle, Mr Kennedy just went missing. He failed to support members of his shadow cabinet against left-leaning traditionalists at the party's conference in the autumn, and tales of his failure to turn up for things multiplied. Then, before Christmas, 11 of his front-bench team signed (but did not deliver) a letter saying that he was doing a bad job.

But still Mr Kennedy didn't go. In the end, it took the threat of exposure on the evening news to prompt his public confession, and even then he seemed to be bidding for sympathy rather than clearing the decks. But his colleagues had had enough and, amidst cries from some of disloyalty, 25 MPs said publicly that they would no longer accept his leadership.

If the Lib Dems are lucky, getting rid of Mr Kennedy may herald an upturn in their fortunes. But it is also possible that, like George III, they will come round from their fever, find much of their territory gone and be unable to repair the mischief.

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Tube strikes

Militant tendency

Jan 12th 2006
From The Economist print edition

The transport unions' hardline tactics are irritating but bring results

Get article background

TOURISTS and residents alike know that London's underground railway can be frustratingly unreliable. This is partly due to decades of underinvestment, which the public-private partnership is supposed to fix. But even when the equipment is working, the staff often aren't. Strikes (real or threatened) on the Tube are a depressingly familiar part of London life. The two most recent—one on New Year's Eve, one on January 9th—followed the familiar script, with the Rail, Maritime and Transport Union (RMT) and London Underground (LU) blaming each other for the woes suffered by the travelling public.

Technology lies at the root of these strikes. Increasing automation makes it possible to run the tube with fewer staff. In 2004 the RMT secured a deal that protected jobs, on the understanding that ticket-sellers—less needed now that many passengers use a pre-paid pass—would be re-assigned to other duties. It now accuses London Underground of going further with redeployment than it said it would.

In the event, and despite dire warnings of chaos, neither strike was terribly effective (although a third, unrelated strike by train drivers from ASLEF, another union, caused misery on one line). Only a few stations were closed, and, according to LU, many staff turned up anyway. Unabashed, the RMT has said it intends to ballot all its members for further action in January and to shut down the network.

But the strikes' limited scope did little to mollify feelings. Business groups and politicians lined up to condemn them. One group of passengers, frustrated by repeated strikes, has taken to boycotting the Tube. Even Ken Livingstone, London's left-wing mayor, is exasperated.

Tube workers have a reputation for being strike-happy. The union militancy of the late 1970s is still well within most grown-ups' memory in Britain, and any hint of its return is unwelcome. Bob Crow, the ex-Communist leader of the RMT, is a man cast in the old mould. A fan of Arthur Scargill, the fire-breathing leader of the miners whose great strike, broken by Margaret Thatcher in 1985, marked the end of union might, he makes no secret of his impatience with the conciliatory tone adopted by many unions thereafter. His union has threatened to strike for all sorts of reasons, from worries about safety after the July 7th bombings to support for a colleague who was sacked for playing squash while off work with an ankle injury. Strikes have been threatened on each of the past three New Year's Eves.

Such hardline tactics are both worrying and effective. The Tube carries 3m people a day and it is well within the unions' power to disrupt the capital. Most strike threats remain mere threats, but even hints of disorder have borne fruit. London's bus drivers, who work in a competitive market where unions have less power, earn up to £25,000 ($44,000), including overtime. Tube drivers, by contrast, make £35,000 a year and get up to 43 days holiday. Station staff earn £21,000—slightly less than the national median—but, thanks to generous leave arrangements, work far fewer hours than most. At a time of generally falling union membership, the RMT is one of the fastest-growing in the land.

London Underground has said that it will stick to its guns. Given the power that the union wields, it will be impressive if managers win the fight over work rosters. One thing only seems certain: more misery for the passengers who pay for it all.

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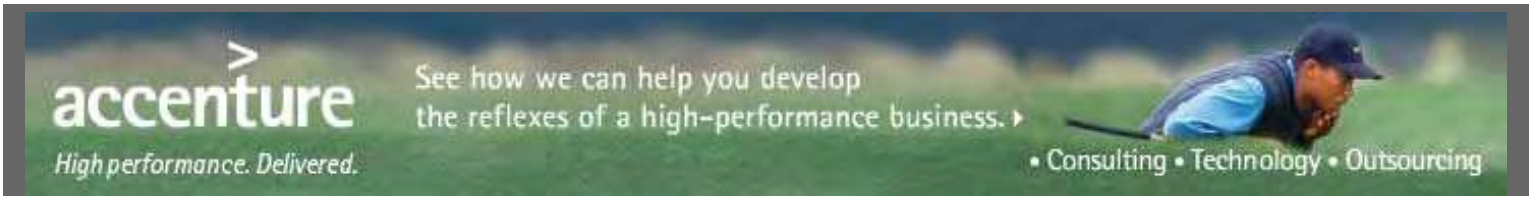
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Failing schools

Off with their heads

Jan 12th 2006
From The Economist print edition

How to improve school performance

ALL the prattle about school choice, beloved of New Labour and Tories alike, is meaningless to a child who ends up with no choice but to attend a failing school. And although failing schools are less numerous than they once were, there are still a lot of them around: 1,557, according to the National Audit Office (NAO), educating nearly a million children. In a report published on January 11th, the government's spending watchdog looks at what causes schools to fail their pupils, how much is spent on turning poor schools around and how effective those efforts are proving to be. Could do better, they conclude.

The government spends around £1 billion a year on a plethora of programmes aimed at stopping schools from sliding into failure and fixing those that do. By far the most expensive is the programme to set up academies in poor inner-city neighbourhoods. The cost is about £27m per school, most of it for fancy new buildings. Fresh Start, under which a school is closed, tarted up and reopened on the same site with new staff and a new name, spends around £2.2m per school. Excellence in Cities gives money to schools in poor areas, and a bad report from school inspectors brings money, too.

In the short run, all this spending does seem to improve exam results. But the value for money is more questionable. Even before the extra funds that come from these programmes, schools that perform poorly offer some of the most expensive education in the state system. They are often half-empty, as students leave if they can find places elsewhere. Although some funding will go with them, not all does, so an unpopular school will end up with more money per student than a popular one. And the targeted spending that comes with failure is sometimes good money thrown after bad. Two-fifths of the schools that came out of “special measures” (the worst grade a school can get from the inspectors) between April 1995 and March 1997 had closed by July 2005.

A recent paper from Policy Exchange, a think-tank whose views command the attention of the new Tory education team and even of some in government, takes a different approach. The authors criticise the current system for rewarding failure and focusing on cost, rather than value. All educational funding should be doled out per head, so that schools have a strong incentive to attract extra students and aren't cushioned from their own mistakes as student numbers fall. And extra spending should go to students who have been failed, rather than schools that are failing.

Students at schools that have been found wanting should be awarded an “advantage premium”—extra money that they could take to any school they choose to attend, even a private one. The funding could be found by scrapping the current government schemes, which throw money at those schools that have shown they cannot be trusted to spend it wisely.

Alan Smithers, an educational expert at the University of Buckingham, agrees that targeting spending on schools, rather than students, is the wrong thing to do. Over time, schools that have money lavished on them will attract more able students, exam results will get better and they will appear to have “turned around” even if there has been no genuine improvement in the quality of education. A recent analysis of city academies supports this view: their exam results are better than those of the schools they replaced, but they also have fewer children on free school meals (the standard measure of student deprivation).

The one thing everyone seems to agree on is that a good head teacher is vital. The NAO found that in two-thirds of the schools criticised by inspectors and later given a clean bill of health, the head had been replaced in the meantime. (They also point out that a good deal of the money spent turning around a failing school goes on severance pay for sub-standard senior staff.) Policy Exchange recommends that heads of failed schools be summarily dismissed and new management brought in, with incentives for success and fines for failure. Mr Smithers agrees, but sounds a note of caution. A school head is like a football manager, he says: a good one can

make a difference, but a poor club will never get the results that money can buy the richest ones.

Chris Woodhead, who headed the schools inspectorate between 1994 and 2000 and now chairs Cognita, a private education company, says the debate about how to remedy school failure should have been over long ago. “We don't need report after report on the theory of turning around failing schools,” he says. “It isn't a matter of money; it's leadership first and foremost.” Perhaps what's needed is decapitation on a vast scale. But recruiting a stellar new head teacher is not that easy. A quarter of all headships in state schools are currently vacant—and there is a retirement bulge on the way.

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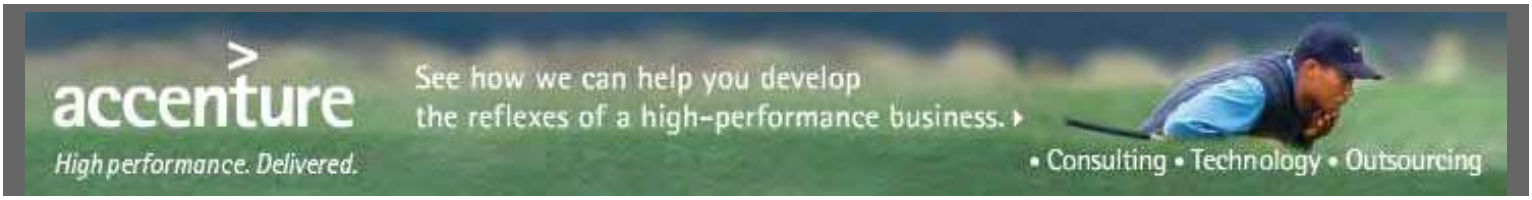
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Retailing therapy

Back to the malls

Jan 12th 2006
From The Economist print edition

But they won't shop till they drop

THE strange death of the British shopper always seemed a fanciful story, even though it has given retailers an almighty fright over the past year or so. Now, Lazarus-like, shoppers are returning to the malls and high streets.

Or they did, at any rate, over Christmas, a crucial period for shopkeepers. According to the British Retail Consortium, the value of “like-for-like” sales (which strips out the effect of increased floor-space) in December was 2.6% higher than the year before. It was the best performance for that month since 2001.

Trading statements by individual stores also point to recovery. Marks & Spencer, for example, a venerable clothing-and-food retailer that has been through a rough patch of boardroom battles and falling turnover, said on January 10th that sales in the Christmas period were “particularly strong”. It reported that like-for-like sales in the 13 weeks to the end of December were 2.9% up on the same period in 2004.

These early indications of a retailing recovery are unlikely, however, to have weighed heavily in the Bank of England's decision on January 12th to keep interest rates at 4.5%. The Bank's rate-setting committee knows that the figures midway through this peak shopping period are tricky to assess. It is unclear whether the momentum from a strong Christmas will carry through to the January sales.

Yet the pick-up is consistent with other signs pointing to a retail revival following the Bank's quarter-point cut in interest rates last August. One reason why retail sales faltered from the middle of 2004 is that the housing market was slowing (see chart). In a rising market, houses turn over more often, which boosts high-street sales as buyers equip and furnish their homes. And, more generally, homeowners release some of their increasing housing wealth by borrowing against it.

Since the Bank's rate cut, the housing market has perked up. The number of mortgage approvals for house purchases reached 115,000 in November, higher than the average monthly level of 108,000 over the past five years. House prices rose by 2.1% in the final quarter of 2005, according to the Halifax index.

Previous setbacks to retailing during the past few years have been followed by sharp recoveries. The recent downturn has been the most severe in a decade but a similarly big bounce-back is unlikely. The conditions that have made retailing so resilient since the mid-1990s no longer hold.

First of all, the housing market may be stabilising but the boom is over. Houses remain overvalued and first-time buyers are still priced out of the market. At best, house prices are likely to remain broadly flat for several years to come. That does not augur well for retail prospects.

Then too there has been a steep rise in borrowing, mainly secured on homes. Household debt now amounts to 150% of post-tax income, up from 110% in 2000. With debt so high, the cost of servicing it, including repayments of principal, is onerous for many households even at today's quite low interest rates. And as worries about pensions intensify, the priority for many individuals is to save more.

Nor does the fiscal outlook bode well for retail spending. Gordon Brown seems anxious to avoid a tax-raising budget this spring. But the Treasury is still expecting the income-tax burden to rise this year and next because of fiscal drag, as tax thresholds rise with prices rather than earnings.

Against this background, the medium-term outlook for the high street is unpromising. Retailers may have escaped the worst but they would be rash to expect a return to the best. There are some miracles too great for even the Christmas season.

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Bad for people, bad for profits

Out of the frying pan

Jan 12th 2006
From The Economist print edition

Eating habits in Britain are changing, but some companies are slow to notice

THE foods of our childhood are a bit like old soldiers; instead of dying they just fade away. This week Golden Wonder, the grand old dame of British crispmakers, was placed in the care of administrators after losing market share for a decade. Its demise comes less than a week after the collapse of Canterbury Foods, once Britain's largest maker of beef burgers and pastries for fast-food outlets and school canteens. One corporate failure in a week may be bad luck or bad management. Two look like the beginnings of a trend.

Golden Wonder once ruled Britain's crisp market. It was the country's leading brand and operator of the world's largest crisp factory before a precipitous fall. In 2004 it sold just 4.3% of Britain's crisps and snacks. And it mostly has itself to blame.

Just look at its advertising. Golden Wonder relied on marketing that featured a long-haired hippie who likened the firm's crisps to his underwear. Its rival Walkers signed up Gary Lineker, a much-loved, clean-living footballer and saw its market share grow from less than 40% 11 years ago to almost 60% last year.

But Golden Wonder's demise isn't just a study in how not to run a marketing campaign. It is also about a change in British eating habits, and the perils of being slow to adapt. After rising for more than half a century, British crisp sales peaked in 2003 and have since slipped by almost 8%, according to Mintel, a research group. On the face of it, that was not good news for any chipmaker. But the broad trend hides more subtle shifts. Sales of premium products such as Kettle Chips and Walkers Sensations increased between 2002 and 2004, and low-fat crisps sold better too.

True to form, Golden Wonder's response was flatfooted. It used posters ridiculing a top-selling Kettle flavour: “Crushed sea salt and balsamic? That'll be salt and vinegar then.” Guess who's laughing now?

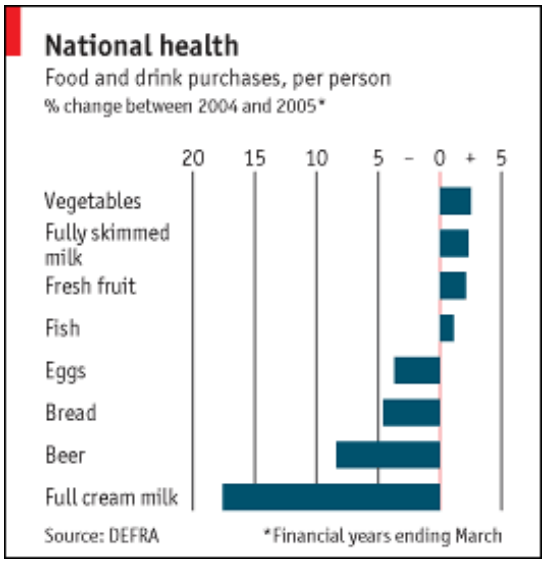
Canterbury Foods was also slow to spot changes. When administrators took charge of it last week, blame was quickly placed at the feet of Jamie Oliver, the young celebrity chef who began in 2004 a campaign to improve school lunches, one of Canterbury's markets. In fact, the company's problems ran deeper than that amiable cook, and included burdensome debts and an inability to compete with more highly-integrated meat processors abroad. In 2002 Canterbury lost a contract to supply patties to Burger King, at the time its largest customer.

Even so, the impact of Mr Oliver's struggle to feed children more vegetables and fewer Turkey Twizzlers cannot be written off entirely. One measure of the reach of his campaign is found in the income statement of Compass Group, the world's largest catering company, which posted a 1% drop in food sales to British schools in its past fiscal year. For this and weightier reasons—including a UN investigation into its murky bidding practices abroad and heavy hand-outs to its top executives—Compass's share price has fallen by 7% over the past four months.

Canterbury laments that when children traipsed back to school in September the usual spike in demand for sausage rolls didn't happen. And the slump is on in homes as well. Per head of population, purchases of ready-to-eat pies and sausage rolls fell by 34% in the two years to March 2005, according to the government's annual Expenditure and Food Survey. Instead, as the chart shows, households are buying more healthy foods, including fish and vegetables and skimmed milk.

The reason isn't hard to find. Some two-thirds of women and 55% of all adults said they felt overweight at some time in the past year, according

to Mintel, while 11% of those surveyed by the Institute of Grocery Distributors admit to feeling guilty each time they snack.



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China

Are you being served?

Jan 12th 2006 | HONG KONG
From The Economist print edition

Imageinechina

China's services sector is escaping from the shadow of manufacturing, but not as fast as it could

Get article background

THE world's factory, it turns out, has a sizeable canteen attached, not to mention an office block and shopping mall. Last month's official revision of China's gross domestic product revealed an economy worth 16 trillion yuan ($1.9 trillion) in 2004, 17% more than previously thought. Some $265 billion of the increase—93% of it—was ascribed to the services sector. As a result, services' share of the economy has jumped by nine percentage points, to 41%, compared with 46% for manufacturing and 13% for primary industries (mainly agriculture and mining).

Where has all this extra activity come from? The bulk of it is obvious to any traveller in China. As people grow wealthier, they want more restaurants and bars, clothes stores, car dealerships, bookshops, private hospitals, English language classes and beauty salons. In many of these businesses, however, turnover and profits have not previously been captured by a statistical system geared to measuring factory production. The small, often private, companies that dominate these areas have also often been at pains to escape notice—and therefore taxes.

Li Deshui, commissioner of China's National Bureau of Statistics, confirms that most of the newly unearthed GDP comes from three categories. The first is wholesale, retail and catering; the second, transport, storage, post and telecommunications. While postal and telecoms services are still state-controlled and thus readily measured, more than 1m small trucking and removal companies are not. The third activity is real estate, booming particularly in the coastal cities and increasingly inland too, leading to an influx of private money—not least from overseas speculators. Property development has, in turn, boosted demand for architects, decorators, do-it-yourself stores and other building services.

But there is more to China's services boom than dishing up stir-fries, shipping boxes and fitting out apartments. Recent years have seen a surge in media and technology services, including the internet; in financial services such as leasing; and in education and leisure. In a small way, for example, China is starting to rival India as an outsourcing hub: less for call-centres that require excellent English than for such tasks as preparing reports and patent filings. In October Microsoft took a stake in a Chinese software firm in Dalian, a city in north-east China with a thriving outsourcing industry preparing tax returns and software for companies from Japan and South Korea.

China's rapid economic growth is fuelling demand for accountants, lawyers, bankers and all manner of consultants,

as Chinese companies expand and restructure. Specialists in marketing, advertising and public relations advise on the relatively new area of marketing products and developing brands. The new wealth has other consequences, too. China now has nearly 1m security guards. And it can offer its new rich everything from cosmetic surgeons to pet salons (see article).

Meanwhile, a huge new market is opening up for private education—fuelled by the combination of a poor public system, the preoccupation of middle-class parents with giving their (often) only child the best chances, and demand from business. Chinese families spend more on education than on anything except housing—the market for courses, books and materials more than doubled from 2002 levels, to $90 billion in 2005. Richer households have also caused a tourism boom, which is still chiefly domestic, though more mainlanders are venturing overseas as visa restrictions are lifted. The World Travel & Tourism Council predicts that China's annual tourism market will more than triple to $300 billion within a decade.

China's services sector, on this basis, is well-developed and roughly as large as those of Japan, South Korea and Taiwan were at a similar stage of development, notes the HSBC bank. In reality, it is bigger still, since the GDP revision cannot capture activities such as kerbside lending and tax-dodging cash transactions in property or entertainment—all of which Dong Tao, chief Asia economist at CSFB, another bank, reckons add another $220 billion to the economy. Even so, the 41% of GDP claimed by services in China remains below the 60-75% typical in developed countries. It is smaller even than India's 52%.

One reason for this is a Communist bias towards manufacturing—“China's ‘real-men-make-stuff' attitude,” as Gordon Orr of McKinsey's Shanghai office puts it. This has led to a plethora of ill-thought-through regulations for services, made worse by China's continuing suspicion of private business, which is mostly concentrated in the services sector. The lack of a national trucking licence, for example, means hauliers must get approval from each province to move goods across the country and unload them on to different trucks at each border—delaying delivery and increasing spoilage and pilfering. In retailing, local governments often maintain inefficient supply chains, in part to protect local jobs. David Wei, head of B&Q in China, says his 48 do-it-yourself stores on the mainland are served by 1,800 suppliers, compared with 600 suppliers in Britain for more than 300 stores.

Worse, though China took an early decision to invite foreign direct investment into manufacturing, it has been reluctant to open up services. Diana Farrell, director of the McKinsey Global Institute, the consultancy's think-tank, argues that allowing more foreign investment in services could bring “not just capital and technology but a competitive dynamic...The presence of Carrefour and Wal-Mart leads to domestic copycats, creating innovation and productivity growth.”

Yet in many services—from telecoms, to the postal service and the media—China thwarts foreign firms with onerous regulations and inconsistent policies. In banking and other financial services, foreigners face limits on ownership and the types of business they can conduct. In legal services, China's severe shortage of lawyers—one for every 13,000 people compared with one for every 300 in America—reflects an impossibly difficult bar exam. Lawyers' poor quality (the practice of bribing judges and rote learning of law means few can argue a case) could be helped by training from foreign firms. Yet foreign lawyers are barred at every turn. They cannot practise or comment on Chinese law, cannot appear in a Chinese court and must wait nine months to open their first office and three years for each subsequent one.

A shortage of well trained people—a complaint of almost every foreign multinational—is also holding back services growth. Many Chinese employees, even qualified graduates, think rigidly rather than creatively and do not challenge authority or ask questions. That may be appropriate in a factory, but not when the client wants to find a clever way to win this contract or that licence.

As long as planned-economy thinking sees services as only an adjunct to manufacturing, China will create fewer jobs in services than it could. Despite its rapid growth, China has shed 15m manufacturing jobs since 1995 and will lose more as basic production moves to even cheaper countries, such as Vietnam. Services could create enough opportunities for the 10m-15m Chinese who are joining the workforce each year. But to fulfil their potential, service industries need more respect and attention from policymakers.

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Pets in China

Friend or food?

Jan 12th 2006 | YANGSHUO
From The Economist print edition

The Chinese learn to love animals in a whole new way

DANGLING on a hook between the chickens and pigs at Yangshuo's central food market is a skinned, boiled dog, teeth bared. In a tourist town in Guilin province better known for its breathtaking mountains, river-rafting and stylish cafes, the sight seems incongruous.

Yet the Chinese have always had a refreshingly unsentimental attitude when it comes to animals. On the mainland, anything that can be eaten usually is. At Yangshuo market, customers barter for every conceivable animal part—feet, brains, lungs, throat, testicles. At banquets, guests might be served such delicacies as moose forehead or deer's penis. And though South Korea gets the bad press, China is the world's biggest consumer of dog meat.

But rising living standards are helping to improve the lot of China's animals. Pets have become a fashion accessory in rich cities like Shanghai, Beijing and Dalian. The number of licensed dogs in Beijing has surged from 130,000 to 410,000 in just a year, reflecting higher incomes and lower licence fees. Including unlicensed mutts, Beijing alone is home to more than 1m dogs. Some speculate that China's “one child” policy has increased the demand for pets.

The better-off sleep in $200 kennels and eat gourmet meals. Gucci is doing a lively trade in designer dog collars. At the more prosaic end of the market, sales of dog and cat food are also soaring. Nestlé, the world's largest producer of pet food, recently announced that it is planning to open its first pet-food factory in China. Pet stores, pet hospitals and animal training courses are sprouting up to serve China's growing army of pooches and moggies. In September the eighth Pet Fair Asia was held in Shanghai, drawing 260 exhibitors and around 80,000 visitors. The market for pets and pet-related products in China now exceeds 15 billion yuan ($1.8 billion).

Such is the potential for new jobs and tax income that China's Ministry of Civil Affairs has created a “Pet and Related Product Development and Service Centre”. With the world's eyes on China as the Beijing Olympics looms, the country is touting its concern about animal welfare as a mark of a civilised society. Even eating dogs may be becoming slightly less socially acceptable. In 2004 ParknShop, part of the Hutchison Whampoa conglomerate, was shamed by a Hong Kong-based animal-rights group into pulling dog meat off the shelves of its supermarkets in southern Guangdong province.

But while animal rights in China are improving, life for much of its human population remains largely nasty, brutish and short. Safety standards, health and lives continue to be sacrificed in the country's pursuit of economic growth. Pollution is taking a serious toll. Some 370 workers a day die in industrial accidents. For such people, at least, it still seems to be a dog's life.

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Patents

Innovation and its enemies

Jan 12th 2006
From The Economist print edition

The world's most inventive companies

JUST as all politicians favour peace and prosperity, so all companies believe in innovation. A rough league table of the world's most intellectually creative firms was published this week, when the United States Patent Office issued its annual rankings of who received the most patents in 2005. IBM claimed the top spot for the 13th consecutive year (but with 307 fewer patents than in 2004). As in previous years, American firms were the minority on the top-ten list, with Japanese computer and electronics firms dominating—in part because of their tradition of filing many applications with narrow claims.

Thinking big
Top US patent recipients, 2005 (preliminary)

Company	Number of patents	1995 rank
IBM	2,941	1
Canon	1,828	2
Hewlett-Packard	1,797	19
Matsushita	1,688	8
Samsung	1,641	21
Micron Technology	1,561	158
Intel	1,549	33
Hitachi	1,271	7
Toshiba	1,258	6
Fujitsu	1,154	12

Source: US Patent and Trademark Office

Strikingly, half of the firms in the top ten were absent from the list a decade ago, showing that the world of innovation is fluid and that no company can presume to maintain leadership forever. Moreover, Microsoft (with around 750 patents) failed to break into the top ten—but with over 13,000 applications pending, it seems bound to get there soon. For now, the firm ranks 18th.

Topping the patent list can be a badge of pride. But garnering a plethora of patents does not necessarily mean that a firm is hugely innovative: the brute number says nothing about the value of the inventions. Fewer than 10% of patents have economic worth. In fact, an increasing number of patents are of dubious merit—and their vigorous assertion can seem a bit like extortion. The infringement case against the maker of BlackBerry wireless e-mail devices will ultimately rest on whether the patents are even valid.

While the European Union frequently berates itself because EU companies register few patents compared with their American peers, many Americans now believe that patents—which let the holders exclude rivals from using a technique for around 20 years—are being issued too freely. As the number of patents grows, even many of the technology firms that rely most on intellectual property have come to believe that the system needs thorough reform.

Part of the reason for the increase in seemingly illegitimate patents is that America's patent office (like most others) is flooded with applications. It now takes around three years for a patent to be approved, and today's backlog of 500,000 is expected to double by the end of the decade unless there are big changes. Annual legislative proposals by Congress stall. Meanwhile, over the past decade the number of patents grew by almost two-thirds, while the amount of patent litigation roughly doubled—fuelled in part by software patents. In 2005 the number of patents issued declined by 12% from a year earlier, though it is unclear if this is a sign that the patent office is working more slowly, or getting stricter.

In an attempt to limit questionable patents, America's patent office said this week it would co-operate with open-source software firms and IBM on an initiative to improve the examination process. It will make it easier for the public to submit materials related to pending patent applications, including any details that could scupper an application. Open-source relies on intellectual property—but uses copyrights, not patents, to stipulate sharing rather than keeping things proprietary.

Software patents are to open-source projects what kryptonite is to Superman. Protecting against them is one of the main motivations for revising the General Public Licence for free and open-source software, a task that formally begins on January 16th at the Massachusetts Institute of Technology. That has its ironies. Open-source software, be it the Linux operating system for servers or the Firefox web browser, is used in nearly all large companies and

government systems: many of the lawyers and techies convening to stymie software patents at MIT next week will be from firms that patent the most.

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Mergers and acquisitions

I like to be in Amerika

Jan 12th 2006 | FRANKFURT
From The Economist print edition

German companies are looking across the Atlantic again

BASF, a German chemicals giant, is courting Engelhard, an American catalyst-maker, in a bid that may turn hostile. ThyssenKrupp is in a bidding battle with Arcelor of Luxembourg for Dofasco, Canada's biggest steelmaker. Last year adidas-Salomon bought Reebok, a rival sports-shoe firm, for $3.8 billion. And that is just a few of the German companies to have been shopping in North America.

With luck this new wave of German transatlantic acquisitions will be managed better than the last. Deutsche Telekom, DaimlerChrysler and the power utility RWE have all had problems with the American companies they bought at the turn of the century. Deutsche Telekom probably overpaid for VoiceStream in 2000. DaimlerChrysler has now mastered cost and quality problems at Chrysler—only to find similar problems are now plaguing its own neglected Mercedes brand at home. RWE gobbled up water companies in 2000, including American Water—but now wants to sell.

Today's deals are smaller and mostly less risky. BASF sees Engelhard as an expansion of its own catalyst business, which would also make its whole portfolio less vulnerable to the economic cycle. As *The Economist* went to press the two companies were haggling over the price: BASF had offered $37 a share, or $38 if Engelhard opens its books. Engelhard told its shareholders not to respond. ThyssenKrupp, by contrast, is seen as a white knight in its $3.5 billion bid for Dofasco, which would complement its existing portfolio of 16 Canadian companies.

Adidas-Salomon's acquisition of Reebok last August was also friendly, but it represents a higher risk for the German company. Although the two firms are in the same business, it will be a challenge to integrate them without damaging the value of either brand. Jochen Zeitz, chief executive of Puma, adidas-Salomon's rival from the same hometown in Bavaria, believes there is more mileage for him in pushing Puma's single brand around the world. Acquisitions are on Puma's agenda too, but only small ones that would add no more than 10% to annual sales. Last month it bought Unisol, which has the Puma licence in Argentina.

The fortunes of TUI, Europe's biggest tourism company, are rather different. It bought CP Ships, a Canadian container company, for $2.4 billion in August last year, to add to the operations of its shipping subsidiary, Hapag-Lloyd. The deal puts Hapag-Lloyd among the world's top five container operators, which are enjoying huge growth in demand. Some analysts feel, however, that TUI overpaid, because it was determined to find a counterbalance for its underperforming tourism business. Other German adventures in North America over the past year include the purchase of Renal Care Group by Fresenius Medical Care, and two acquisitions by Siemens, of US Filter and CTI Molecular Imaging. SAP, a huge German IT company, has joined the fun—buying Khimetrics, which sells price-optimisation software.

So should the heirs of Paul Revere in American boardrooms be shouting, “the Germans are coming”? Not quite—given the relatively small scale of this wave of acquisitions. But there is clearly a new German interest in buying into America, driven by healthy balance sheets at home, higher profits and a feeling that companies that want to be multinational must be in America. Martin Koehler at Boston Consulting Group thinks that German companies may be too eager to join the party. He worries that they risk over-paying by buying now while prices are high, boosted by a buoyant stockmarket.

Jürgen Hambrecht, BASF's chief executive, admits that it would indeed have been cheaper to bid for Engelhard a year ago, particularly given shifts in the exchange rate. But, as he sees it, that simply underlines the strategic nature of the bid: BASF reviewed its portfolio last year and decided Engelhard would fit. The planned acquisition is not about a desire to be in the United States for its own sake, says Mr Hambrecht. “This is a global business.” Buying Engelhard is part of BASF's plans for the next ten years to number in the top three in its core businesses, he insists.

BASF, like many global German companies, has weaned itself off its dependence on the German market, although it retains a big base in Ludwigshafen. Puma has not made things in Germany for the past 13 years, because of the cost. Its German operations consist of product development, design and marketing. It has split its operational headquarters between Germany, Hong Kong and North America.

If the new German government inspires confidence, and internal—particularly consumer—demand picks up, German companies may be more inclined to spend money back at home. For the moment, however, much of corporate Germany will continue to think about expanding abroad. But listed companies, even giants with well known long-term strategies, have to be mindful of their investors. The stockmarket has not liked BASF's bid for Engelhard (though Mr Hambrecht says he expected as much). The gung-ho euphoria of the late 1990s has evaporated. German companies that spend money in North America today are expected to have done their homework rather better than their predecessors.

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Apple

Podtastic

Jan 12th 2006
From The Economist print edition

The iPod has turned Apple into a superbrand

IT WAS on millions of wish lists over the holiday season and few other brands got a look in. In the three months to December 31st, Apple sold 14m digital music players, compared with 4.5m in the same period in 2004. The iPod defines a product category, as Sony's Walkman once did when music was delivered on cassette instead of over the internet. And with Apple's iTunes Music Store accounting for 80% of legal music downloads, the Californian company now has a brand that marketers hold in awe. But can Apple also use its new brand power to sell more computers?

At Apple's annual Macworld event on January 10th, Steve Jobs, the company's chief executive, unveiled what many fans had been expecting: the first Macintosh computers based on chips made by Intel, which also power the vast majority of personal computers that run Microsoft's Windows operating system. Apple hopes the high performance of its new Intel-based Macs will help it take market share from makers of Windows-based PCs.

But the “halo effect” from the iPod remains Apple's most effective means of boosting sales of its computers. Surveys suggest that some 10-20% of PC users who buy an iPod subsequently go on to buy a Mac. In 2005 the iPod helped the company to increase its share of the personal-computer market from 3% to 4%. Apple's challenge is that getting people to buy an iPod, a new type of device, is easier than getting them to switch loyalties in an existing product category.

The most powerful factor working in Apple's favour is peer pressure: what friends and relatives have to say about products is now the most trusted form of consumer advice, and to be seen with something different can be almost taboo. That is why millions of people said they wanted an iPod for Christmas, and not a digital-music player from another manufacturer—even though rival players are often cheaper than iPods, and generally have more features. During the years it spent in Microsoft's shadow, Apple benefited from having a distinctive, counter-cultural brand. But given its dominance in digital music, where it is anything but the underdog, how long can Apple keep its cool?

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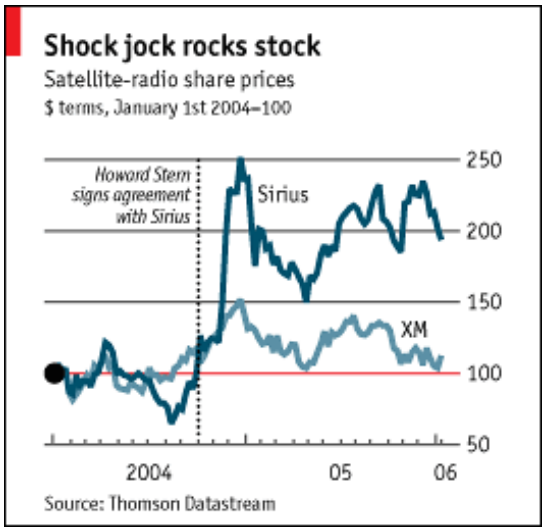
Satellite radio

Howard's way

Jan 12th 2006 | NEW YORK
From The Economist print edition

Satellite radio comes of age

"IN ONE astonishingly audacious fantasy", the *Chicago Tribune* reports, "an impersonator of David Letterman—dubbed Evil Dave—engaged in a phone-sex sketch involving descriptions of Martha Stewart and certain anatomically impossible events." American radio listeners will recognise instantly here the world of Howard Stern, America's sleaziest and most popular radio host. On January 9th Mr Stern re-launched his show on a subscriber-only satellite radio network, Sirius, after leaving CBS Radio (formerly known as Infinity Broadcasting), last month.



The return of Mr Stern and his regular guests—"a cast of Wack Packers, Farters, Strippers and Porn Stars", as Sirius calls them—was a national event, and subscriptions to Sirius, costing $12.95 a month, soared in anticipation. Sirius ended 2005 with more than 3.3m subscribers for its 125 channels of talk and music, against just 660,000 subscribers when it signed up Mr Stern in October 2004. Held back by his contract with CBS, he used the extra months there to plug Sirius relentlessly.

The publicity his move generated for satellite radio helped not only Sirius, but also its bigger rival, XM Satellite Radio, which ended 2005 with almost 6m subscribers. Both started broadcasting less than five years ago. Their combined 9m subscribers is twice the number they had a year ago, and they expect about 15m in a year's time. By embracing satellite radio Mr Stern has helped to turn it from a novelty product into a mainstream one—whatever that may say about American taste.

Mr Stern has also turned around perceptions of Sirius, which began broadcasting after XM and has lagged behind ever since in market share. To get Mr Stern's show, Sirius promised to pay $80m a year and to give company stock then worth $100m to Mr Stern and his agent—even though it had barely $1 billion in shareholders' equity at the time and was losing money heavily. Had so many of Mr Stern's 12m listeners not followed him from CBS to Sirius, the deal could have sunk both Sirius and Mr Stern.

Reuters

Shaggy host story

In the event, Mr Stern's pull has been so strong that by the time Sirius gave him the promised stock last week, it was worth $220m. Sirius's share price has risen from a low of $2 before the Stern deal to well over $6 today—valuing the company at $8.2 billion, or one-quarter more than XM, even though XM is almost twice as big in terms of subscribers and revenues.

That may be too much of a good thing. Goldman Sachs said last week it still thought XM the “superior investment” in the sector. And, Mr Stern aside, there is not all that much to distinguish Sirius from XM, save for its sports coverage. Sirius has a deal with the National Football League, XM with Major League Baseball. Beyond that, the two stations shade off in a scattering of channels hosted by diverse celebrities (XM has just signed Bob Dylan), and scores of all-music channels dedicated to different genres, or even single artists. The talk channels carry advertising; the music channels do not.

Craig Moffett and Amelia Wong, analysts with Sanford C. Bernstein, see much prosperity ahead for both firms. They say that XM and Sirius look set to enjoy a duopoly in their industry “similar to Coke and Pepsi”, with high profit margins and barriers to entry. They forecast a market of 44m satellite subscribers by 2010, divided more or less equally between the two providers.

That may sound a bit optimistic, but satellite radio is proving a big hit with American consumers once they get over the idea of paying for it. The “churn” rate (of dissatisfied subscribers who drop the service) is barely 1.5% a month for Sirius, which the company reckons to be among the lowest for any subscription business. “Our programming is so compelling, and so sticky, and so strong”, said Mel Karmazin, Sirius's chief executive, this week. And with Howard Stern on board, who could disagree with his choice of words?

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Luxury-car clubs

Ferraris to go

Jan 12th 2006 | NEW YORK AND LAS VEGAS
From The Economist print edition

Time-shares for high-end cars are catching on

AN HOUR after Wall Street closed one recent Friday, a youngish man in jeans and a sports jacket strode into the showroom of the Classic Car Club of Manhattan, a few blocks north of Tribeca. He paced between an Aston Martin V8, a Rolls-Royce Corniche, two vintage Ferraris and a dozen others, eager to find something for a night out. Ten minutes later he zipped through the hangar doors in a 2005 Lotus Elise, a bright-red, curvy little number. There was no bill to pay and no insurance form to sign.

Luxury-car clubs are well established in Europe. Now they are catching on in the United States. The idea is that for an annual membership fee, plus (sometimes) a weekly charge, members can have their choice of smart cars. Ron Van Horssen, who recently opened a club near Phoenix, says the model is based on executive-jet sharing. Rich people, he thinks, are realising that “owning an asset is not necessarily the best way of getting the benefits of using it”. A spin in a Van Horssen Ferrari Maranello costs $4,500 per week, plus the $7,000 annual fee. No one needs to worry about maintenance or inspections—and, as price tags on new Lamborghinis and Bentleys have climbed, the rich can even save a bit of money.

Only a handful of clubs exist now in America, and none has national scope. Club Sportiva, a pioneer when it opened three years ago, is in San Francisco and San Jose; Exotic Car Share is in Chicago and New York. The Classic Car Club, a British firm, opened its Manhattan branch last July. But most are looking to expand. Torbin Fuller of Club Sportiva predicts that: “We'll be national here in the next two to three years.”

A variant on the formula is offered by exotic rental-car companies, which have no annual membership fee, and rent out cars for a day or a week. They are growing too. Dream Car Rentals, a Las Vegas firm with a fleet of 140, is opening a new branch at Fisherman's Wharf in San Francisco. Many of the company's Las Vegas customers are Europeans, and female clients come in only “once in a blue moon,” says Gavin Mate, a manager.

The mainstream rental-car companies have also spotted the trend, and are determined not to be left behind. In 2001 Hertz launched its “Prestige Collection”, with Jaguars and Lincoln Navigators and special services such as free pick-up. That business, claims Hertz, has been an “unmitigated success” and continues to expand. Enterprise, the largest rental company in North America, reports a nearly 45% jump in luxury-car rentals in the year to October 2005. And with Wall Street bonuses soaring, 2006 is looking pretty good as well.

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Face value

St Lawrence of Google

Jan 12th 2006
From The Economist print edition

Getty Images

Larry Page, the co-founder of Google, has always wanted to change the world. He is well on his way

DOES Larry Page ever get vertigo when contemplating his life and future? After all, Mr Page and Sergey Brin, the co-founders of Google, the world's most popular internet search engine, can legitimately claim to have caused an information and media revolution. At 32, they are already worth far more than $10 billion each and fly around in their own Boeing 767. Bill Gates fears them; others in the industry admire or envy them, and some seem to consider them capable of anything. Expectations are dizzyingly high.

“It's not a good thing to think about,” said Mr Page behind the stage after his keynote address in Las Vegas at the Consumer Electronics Show (CES) last week. But if he must ponder his company's achievements and power, he says in his halting, thoughtful voice, it gives him an even greater “sense of responsibility” to make the world a better place. “The reason your question doesn't make sense”, adds Eric Schmidt, the comparative veteran who is Google's chief executive and jointly runs the company with the founders, “is that he's too busy” to have vertigo. Busy, that is, changing the world.

That self-avowed goal causes a great deal of confusion. For instance, for the entire week leading up to his Las Vegas speech, much of the world's press decided to believe a rumour that Mr Page would announce a new, cheap computer powered by Google software (thus, went the logic, finally contesting Microsoft's reign over operating systems). Mr Page announced nothing of the sort. Yes, Google will “support” an existing (and well-known) project by the Massachusetts Institute of Technology to produce a laptop for the poor, but so will many companies, and who wouldn't? At one point, Mr Page mocked such inflated expectations by “announcing” Google Fastfood, a button in car dashboards that delivers instantaneous hamburgers.

Mr Page used much of his speech to play the part of visionary geek-in-chief, dressed in a white lab coat and standing on spring-heeled sneakers, exhorting the 2,500 exhibitors at the CES to agree on industry standards and to make their gadgets less off-putting. He did also announce some intriguing new products—such as an expansion of Google Video, a download service that allows anybody to sell videos—thus continuing a seemingly endless dribble of product launches that cumulatively suggest astonishing ambition. Not only is Google already pursuing its stated goal to “organise all the world's information” (not just web pages) by scanning library books to make them

searchable, by bringing local information to mobile phones and people on the go, and so forth; it is also dabbling in side projects such as providing free wireless internet access to its home town in Silicon Valley, and perhaps to San Francisco and beyond.

Mr Page's ambition started early. When he was 12, he read a biography of Nikola Tesla, a prolific inventor who never got credit for much, but is now a hero among geeks. Mr Page decided that he would be different: a great inventor and an acknowledged world-changer to boot. As the son of a computer-science professor, he channelled his energy into technology. By the time he was in college, Mr Page was building working inkjet printers out of Lego bricks—probably just to show that he could. A few years later, while doing his doctoral thesis at Stanford, Mr Page thought up his “PageRank” system of ranking web pages by relevance, the foundation of Google's search engine. Teaming up with his intellectual soul mate, the Russian-born and mathematically gifted Mr Brin, Mr Page went “on leave” from his research and founded Google.

Mr Page was chief executive, until the founders were advised that they needed a more experienced adult at the helm: hence the arrival of Mr Schmidt, formerly the boss of Novell, a software firm. But Google stayed very much its founders' creation. It was Mr Page who wrote the letter—now legendary—in Google's regulatory filings for its stockmarket listing that announced the company motto: “Don't be evil”. Despite rapid growth—from about 200 employees when Mr Page was chief executive to nearly 5,000 now—Google has lost none of its puritanical fanaticism.

This zeal is starting to annoy some people. One visitor to the company's “Googleplex” in Silicon Valley “felt as if I were in the company of missionaries”. A consequence of the theory that Google is aiming to run the world could be that “Google may be less liked in the industry than Microsoft inside 12 months,” says Pip Coburn, a technology analyst. Bloggers have started accusing Google of hubris and arrogance. Paul Saffo at Silicon Valley's Institute for the Future says that “Google is a religion posing as a company.”

Playing God

If Google is a religion, what is its God? It would have to be The Algorithm. Faith in the possibility of an omniscient and omnipotent algorithm appears to be what Messrs Page and Brin have in common. It's “in their DNA,” says Michael Moritz, a venture capitalist famous for investing early in both Yahoo! and Google. Whereas Yahoo! was started by two Stanford students who turned a hobby into a business, Google was started by two Stanford students who turned an intellectual obsession into a quest, says Mr Moritz. And what is that quest? Merely upstaging Microsoft would be almost banal. “We're not trying to build a better operating system,” says Mr Schmidt (although that will not kill the rumour). Part of the plan is certainly “organising the world's information”. But some people think they detect an even more grandiose design. Google is already working on a massive and global computing grid. Eventually, says Mr Saffo, “they're trying to build the machine that will pass the Turing test”—in other words, an artificial intelligence that can pass as a human in written conversations. Wisely or not, Google wants to be a new sort of *deus ex machina*.

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Alan Greenspan

Monetary myopia

Jan 12th 2006
From The Economist print edition

AP

The accolades bestowed upon Alan Greenspan ahead of his retirement on January 31st have a strong whiff of irrational exuberance

ALAN GREENSPAN, now in his final weeks as the chairman of America's Federal Reserve, has been proclaimed “the greatest central banker who ever lived”. Among ordinary Americans he enjoys almost rock-star status. He has been awarded the Presidential Medal of Freedom, a British knighthood and the French Legion of Honour. Does he really deserve such uniform praise? And after the accolades have faded, what will economists conclude about his tenure?

It is ironic that when Mr Greenspan took over from Paul Volcker, his inflation-busting predecessor, in 1987, some questioned whether he was really up to the job, and he went through some rocky times in his early years. The stockmarket crashed within two months of his taking office, and America's growth fell behind that of Europe and Japan for several years. For the past decade, however, he has been viewed as possessing almost magical powers. He is credited with saving the world economy—from the stockmarket crashes of 1987 and 2000-01, and from Russia's default and the near collapse of LTCM, a hedge fund, in 1998—by pumping in liquidity when it was vulnerable. At a dinner for the members of the G7 in December, Mervyn King, the football-mad governor of the Bank of England, presented Mr Greenspan with a cartoon depicting him as a goalkeeper saving one penalty after another.

On the surface, America's economic performance has been remarkable on his watch. Not only has inflation been reduced, but America has enjoyed the two longest expansions on record, marred only by two mild recessions. The previous 18 years, by contrast, suffered four recessions, including the two severest since the Great Depression of the 1930s.

On closer inspection, however, Mr Greenspan's record looks less impressive. The drop in America's core rate of inflation has in fact been no greater than the average for all the industrialised countries in the Organisation for Economic Co-operation and Development (OECD). Global disinflationary pressures have made fighting inflation easier for all central banks.

Nor has Mr Greenspan done a much better job than foreign central banks at smoothing the business cycle. It is

true that America has enjoyed faster GDP growth than other big OECD economies, but that should not be attributed to the Fed. Long-run growth rates are driven by structural factors not monetary policy, which mainly affects output over the cycle. America's potential growth rate is higher than that of the euro zone and Japan, thanks largely to faster population growth and more flexible labour and product markets.

An analysis by Martin Barnes, of the Bank Credit Analyst, finds that if America's growth performance is instead measured by the gap between actual and potential output, it looks much less stellar. America has on average had a slightly larger negative output gap than the rest of the OECD. Other economies have also enjoyed shallow recessions. Indeed, research by two American economists, James Stock and Mark Watson, has concluded that the decline in America's economic volatility over the past two decades was due chiefly to smaller economic shocks or the growing share of services (which are less recession-prone than manufacturing); only one-tenth of the increased economic stability was, they reckon, due to better monetary policy.

The Greenspan fan club claims that the chairman's skilful policies have not only reduced economic volatility, but may also, at least temporarily, have increased America's potential growth rate. Spotting the spurt in productivity growth in the late 1990s before almost anybody else was one of Mr Greenspan's greatest achievements. Recognising that this would allow the economy to grow faster without fuelling inflation, Mr Greenspan allowed the boom to continue and unemployment to fall, dragging many disadvantaged workers back into the labour force.

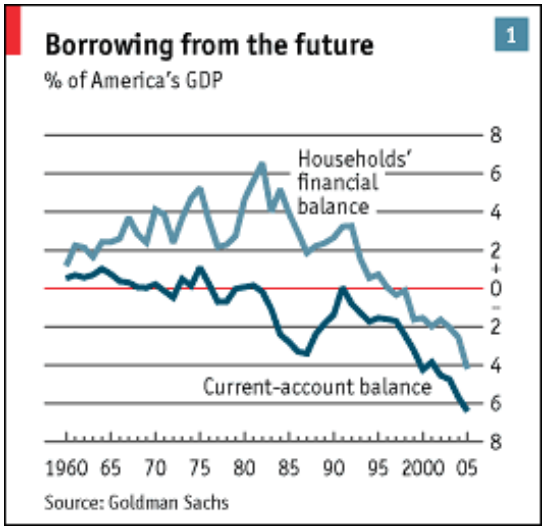
However, this short-term gain came at a long-term cost. His faith in the productivity miracle may have blinded him to the dangers of excessive monetary growth. His policies allowed domestic demand consistently to grow faster than supply, causing America's current-account deficit to swell alarmingly.

On Mr Greenspan's watch, America has also experienced the biggest stockmarket and housing bubbles in history. Presiding over one bubble could be seen as bad luck; presiding over two smacks of carelessness. The Greenspan era will not end on January 31st. Instead, his legacy will linger in the shape of the biggest economic imbalances in American history: a negative household saving rate and a record current-account deficit (see chart 1). Until these imbalances unwind—a process that could prove painful—it is too soon to applaud Mr Greenspan's record.

Toil and trouble

The Economist's long-running quarrel with Mr Greenspan is that he chose not to restrain the stockmarket bubble in the late 1990s or to curb today's housing bubble. He has declared himself vindicated in not pricking the equity bubble with higher interest rates, but instead to let it burst and then cut rates sharply to "mop up" the damage. The economy has fared better than we expected since share prices slumped, with only a mild recession in 2001. But a better test of Mr Greenspan's policies is not whether America escaped a deep recession, but whether the economy would today be on firmer foundations if the Fed had acted against that bubble.

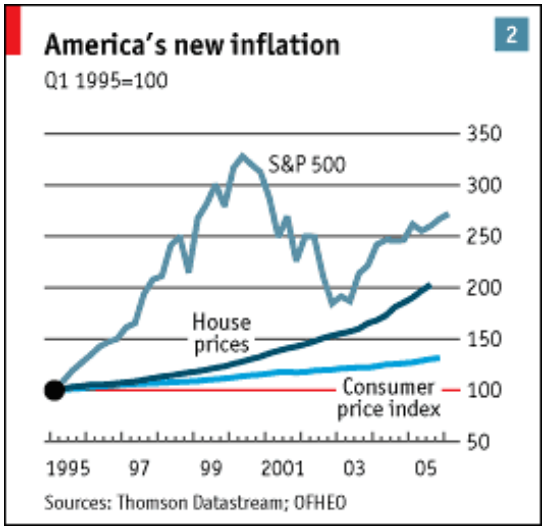
How monetary policy should respond to increases in the prices of assets such as houses or shares is the biggest dilemma facing central banks everywhere. The Fed takes account of rising asset prices to the extent that they boost spending and hence future inflation. But the burning question is: should it respond to asset prices even if inflation seems under control? Three main arguments are given by Mr Greenspan and his colleagues for why central banks should ignore asset prices other than their impact on inflation. First, that monetary policy focused on inflation and growth is the best way to achieve economic stability. Second, that one can never be sure that what looks like a bubble really is a bubble. And third, that interest rates affect the economy more like a sledgehammer than a scalpel. A modest rise in rates is unlikely to halt rising share prices, but an increase sufficient to pop the bubble would slow the whole economy and could even cause a recession. Mr Greenspan thus concludes that it is safer to wait for a bubble to burst by itself and then to ease monetary policy to soften a downturn.



Consider each of these arguments in turn. First, the job of a central bank is not just to prevent inflation, but also to ensure financial stability. Yet the three biggest stockmarket bubbles in the past century—America's in the 1920s and 1990s and Japan's in the 1980s—all developed when inflation was low. Arguably, Mr Greenspan has defined the role of monetary policy too narrowly. Inflation is often described as too much money chasing too few goods. But in a world awash with cheap money and with potent new sources of supply, such as China, to hold prices down, inflation will remain low and so fail to signal if an economy is overheating. Increased central-bank credibility also helps to anchor inflation. If central banks hold interest rates low, this will encourage risk-taking in financial markets and excess liquidity will spill over into asset prices rather than traditional inflation (see chart 2).

Asset-price inflation can be as harmful as conventional inflation. A sudden collapse in share or house prices can trigger a deep downturn. And surging asset prices also distort price signals and cause a misallocation of resources—by encouraging too little saving, or too much investment in housing, so reducing future growth. This is why central banks need to pay closer attention to asset prices.

Second, it is not, as Mr Greenspan argues, impossible to identify bubbles. When prices have lost touch with fundamentals and there are other signs of excess, such as rapid credit growth, alarm bells should ring. Mr Greenspan's "irrational exuberance" speech in December 1996 shows he was concerned about a bubble inflating long before the bubble reached its full extent. And transcripts of meetings of the Federal Open Market Committee (FOMC, which meets to set interest rates) now make clear that several Fed officials were fretting about the bubble in 1998 and 1999. At the December 1999 meeting, when discussing the stockmarket, Mr Greenspan said: "It is only a question of how much of a bubble there is."



Moreover, central banks do not have to be certain they have identified a bubble before they act. Monetary policy has constantly to deal with uncertainty—such as the size of the output gap. Uncertainty is a reason for responding cautiously, but not for doing nothing.

What of Mr Greenspan's third claim that, even if a central banker is pretty sure there is a bubble, there is little he can do about it because interest rates are a blunt tool? In August 2005 Mr Greenspan said: "Given our current state of knowledge, I find it difficult to envision central banks successfully targeting asset prices any time soon." But he was setting up a straw man. Nobody is seriously arguing that central banks should "target" a particular level of asset prices. Most economists accept that aggressive action to "prick" bubbles could also be risky. Instead, the debate today is whether central banks should "lean against the wind" when asset prices appear dangerously out of line with fundamentals, raising interest rates by a bit more than inflation alone would call for.

Beyond inflation

Contrary to what Mr Greenspan said, some central banks are already doing exactly that. The Bank of England and the Reserve Banks of Australia and New Zealand have raised interest rates in recent years by rather more than inflation alone justified, because of concerns about house prices. Mr Greenspan is also wrong to argue that only a big rise in rates can halt a bubble. In both Britain and Australia, rate increases of just 125 basis points, along with clear warnings from the central banks that house prices were overvalued, were enough to slow the annual pace of house inflation from around 20% to close to zero.

Britain's Mr King was one of the first central bankers to lay out the case for why monetary policy may sometimes need to be tightened in response to rising asset prices, even if forecast inflation is within its target range. This, he argues, implies accepting a modest undershoot of inflation in the short term, in order to avoid a bigger undershoot later when a bursting bubble could lead to a deep downturn and even deflation. Jean-Claude Trichet, the president of the European Central Bank, also agrees that central banks should, in exceptional circumstances, tighten policy to restrain asset-price booms, even if inflation is low. This is a justification for the ECB's much criticised two-pillar monetary-policy framework, which focuses on money-supply growth as well as inflation: asset-price bubbles are usually accompanied by rapid growth in money and credit.

Several members of the FOMC argue that in practice the Fed and other central banks have responded to surging house prices in similar ways. The only difference, they claim, is in what they say, not what they do. That real interest rates have been much lower in America than in Britain or Australia undermines this assertion. But in any case, if a central bank wants to influence bubbling asset prices and the imbalances they cause, it needs to speak out. Not only did the Fed raise interest rates too late and by too little in the late 1990s, but instead of trying to talk down the bubble Mr Greenspan acted as a cheerleader for the new economy. Although he was right about faster productivity growth, his exuberance unintentionally encouraged investors' unrealistic profit expectations, pushing share prices still higher.

The deepest flaw in Mr Greenspan's policy towards asset prices is its asymmetry. If the Fed always cuts interest rates when asset prices tumble, but never raises them when they soar, then investors will be encouraged to take bigger risks. That makes bubbles more likely. The Fed was right to ease when the stockmarket bubble burst, to avoid repeating the Bank of Japan's mistake in the 1990s. But such "mopping up" should be a last resort, not a concerted strategy that cushions the bursting of one bubble by inflating another—since 2002, in housing.

Pragmatist, not purist

So a strong case can be made that the Fed's neglect of asset prices has caused it to pursue an overly loose monetary policy. The strange thing is that Mr Greenspan was one of the first central bankers to draw attention to the growing importance of asset prices in economies. In private discussions, it is clear that his views are less rigid than is commonly assumed. Moreover, Mr Greenspan conceded in testimony to Congress in 1999 that “If we could find a way to prevent or deflate emerging bubbles, we would be better off.” And more recently: “I certainly do not rule out that future work could improve our understanding of asset-price behaviour, and with it, the conduct of monetary policy.”

Indeed, Mr Greenspan's public pronouncements on asset prices seem to have changed subtly. Until recently, he denied the possibility of a nationwide housing bubble; now he admits the market is frothy and has warned that house prices could fall. In September a research paper co-written by him drew attention to the massive scale of mortgage-equity withdrawal. He estimates that this could account for all of the fall in America's personal saving rate in the past decade. This implies that a drop in house prices could trigger a sharp slowdown in spending. It was only the second study he put his name to while in office.

In a further shift, Mr Greenspan acknowledged in September that the Fed's policy might have played a role in fostering bubbles. He argued that the Fed's success in delivering a long period of economic stability and low inflation—and hence low interest rates—may have caused investors to demand less compensation for risk, inflating the prices of assets.

Mr Greenspan's new thinking about bubbles would be consistent with the risk-management approach that he favours for monetary policy. This looks not only at the likely path for the economy, but at the risks and costs and benefits of other possible outcomes and policies. Within this framework, tightening monetary policy in an asset boom is like buying insurance against a later risk of a larger economic bust. The cost of some short-term loss of output must be set against the risk of larger future losses if asset prices slump.

Who will save us in future?

From a risk-management perspective, the case for acting against the housing bubble is even greater than for the stockmarket bubble. A housing bubble has bigger wealth effects on consumer spending, so a collapse in house prices would cause more economic harm than one in share prices. Such a bubble is more likely to create financial instability because people borrow more to buy homes. And raising interest rates is a more powerful tool against rising house prices than share prices.

In contrast to Mr Greenspan's pragmatic approach to asset prices, Ben Bernanke, his successor, believes that interest rates should not respond to movements in asset prices unless they affect forecast inflation. Research co-written by Mr Bernanke in 1999 concluded that if a central bank responds to asset prices it risks only creating more economic instability compared with pursuing an inflation target. However, his model assumed that bubbles just happen. In reality, monetary policy can contribute to the inflating of a bubble—not least if investors expect the Fed to cut interest rates when share prices fall, but to do nothing to prevent their rise.

Parting of the ways

Alongside his views on bubbles, Mr Bernanke is keen to introduce a formal inflation target, which could reduce the Fed's room to respond to asset prices. So it would seem that at the very moment when the gap between Mr Greenspan and other central bankers was narrowing, the Fed might unfortunately be about to take a step back under Mr Bernanke.

Mr Greenspan's past reluctance to tackle asset prices is partly understandable: central banks do not have a mandate to pop bubbles. It is therefore hard to justify an increase in interest rates to Congress when inflation is low, as it was in the late 1990s. Nevertheless, views change over time. In the 1960s the main objective of monetary policy was full employment, not inflation. Persuading the public today that asset bubbles are as dangerous as inflation is surely no harder than switching focus from unemployment to inflation.

But first, Mr Greenspan and other central bankers need to start arguing the case for raising interest rates in response to rising share and house prices—and to be prepared to live with the unpopularity that would follow. Mr Greenspan would certainly not be so popular today if he had spoken out and leant more firmly against the

stockmarket and housing bubbles.

Indeed, as the farewell tributes to Mr Greenspan reach fever pitch, ironically it is perhaps his extraordinary popularity and perceived wizardry that best explain the problems he will leave behind. Investors' exaggerated faith in his ability to protect them has undoubtedly encouraged them to take ever bigger risks and pushed share and house prices higher. In turn, American consumer spending has become dangerously dependent on unsustainable increases in asset prices and debt.

In December Mr Greenspan was made a Freeman of the City of London. One of the traditional perks of this honour is that he can be drunk and disorderly without fear of arrest. The snag is that his policies have also encouraged drunk and disorderly asset markets and intoxicated consumers. When the party ends, Mr Greenspan will not be there to clean up the mess. But end it surely will.

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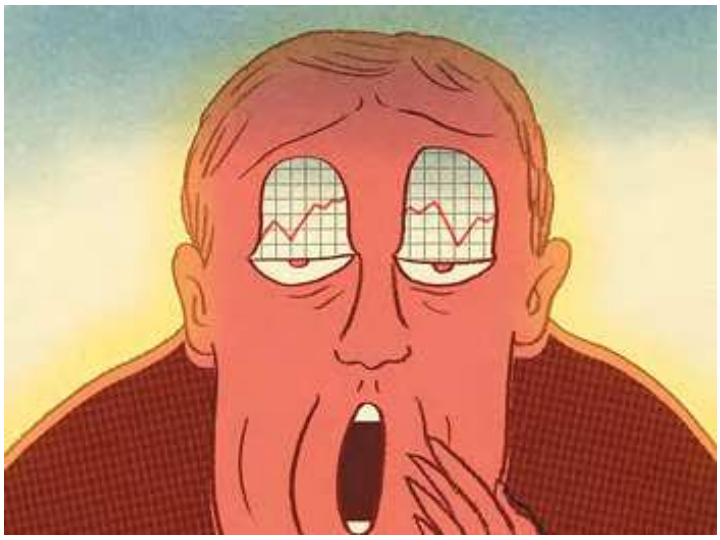
Financial literacy

Caveat investor

Jan 12th 2006
From The Economist print edition



Individuals are taking on more financial responsibility, not least in providing for their old age. Maybe they should be better prepared

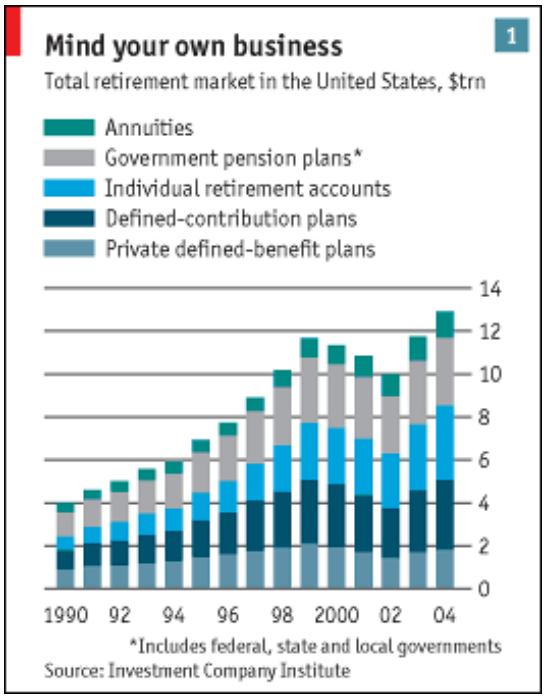
WHEN IBM announced an overhaul of its pension plan for employees in America last week, it joined a parade of employers that are shifting more responsibility for saving for retirement on to workers. For many Americans, of course, this is nothing new: millions of them have been managing their retirement assets in individual accounts for years (see chart 1). Nevertheless, in both America and Britain the closure of paternalistic corporate "defined benefit" programmes, in which pensions depend on earnings and years of service, is accelerating—even at healthy companies such as IBM (see article).

To the extent that this creates and encourages individual choice and responsibility, it is something to welcome rather than to fear. Many other countries, facing huge state-pension obligations, would also like to see their citizens assume a bigger role in providing for their own retirement. Even so, the trend raises an important question: how much do people due to take on these new responsibilities know about basic financial concepts?

The answer seems to be: not much, and less than they think they do. Studies show that many people overestimate their knowledge of everything from inflation to risk diversification and compound interest. One survey in Australia found that 37% of people who owned investments did not know that they could fluctuate in value. In America 31% did not know that the finance charge on a credit-card statement is what they pay to use credit. Britain's Financial Services Authority will release the results of its own survey on financial literacy in the next month or two.

Even educated professionals may know the basics but see no need to keep up to date—having no idea of the interest rates on their credit cards, the fees on their mutual funds or how their investments are doing.

But in both America and Britain low personal saving rates (negative in America, indeed) and record numbers of personal bankruptcies do not bode well. If people are to take charge of their pensions, shouldn't they know a little more?



In the end, ignorance could rebound on governments: if people save too little for old age, the state may have to provide for them willy-nilly. "Governments are taking this very seriously," says Barbara Smith of the Organisation for Economic Co-operation and Development, which recently produced a report on global financial literacy. Just this week the British government launched an online debt calculator for overstretched consumers and a money-management course for teenagers that will be offered in schools across the country later this year. New Zealand is another country trying to catch its people young: one official financial-information website there (www.sorted.org.nz) includes an online game on "Money Island".

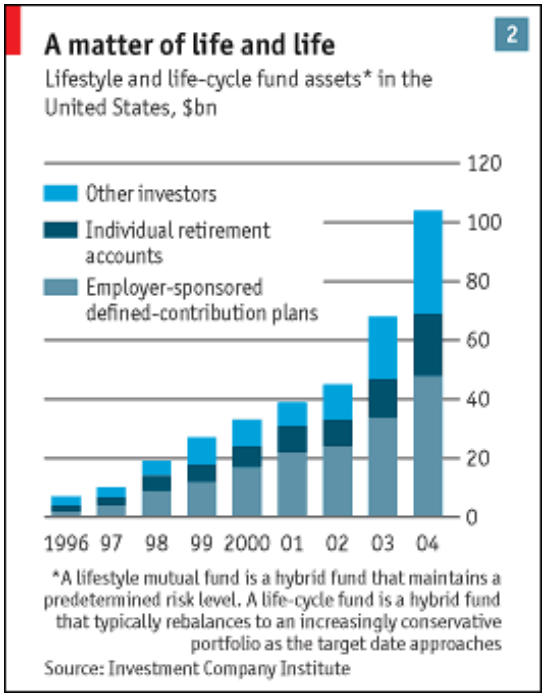
The potential economic benefits of financial literacy extend beyond government budgets. More informed consumers—not just investors—would increase the efficiency of markets and help keep unscrupulous sellers at bay. If financial illiteracy leads to greater debt, then increased consumption today will be at the expense of less later, as interest payments weigh on household budgets.

Once people make financial decisions, they tend to stick to them even if a change might make more sense. Watson Wyatt, a consultancy, says that about half of Britons in defined-contribution pension plans (in which retirement benefits depend on investments' performance) never change the allocation of assets. One-third have not even reviewed them for several years. There is evidence that such inertia is a feature of other financial markets, including the one for mortgages (see article).

America has had a variety of financial-education programmes for some time, generally relying on the private sector. Most large companies and many smaller ones put on investment seminars for their employees, run by outside experts. Many of those who attend these seminars later increase their saving for retirement.

However, there is a fine line between education and advice. Although education and sales are meant to be strictly separated, many of those giving the seminars work for firms that sell financial products. Some employers have been hesitant to sponsor financial seminars for fear of being sued, notes Lynn Dudley of the American Benefits Council, a lobby group. Two bills now before Congress attempt to deal with this question. Meanwhile, a growing number of pension schemes offer "lifestyle" or "life-cycle" funds that skirt the question of advice by automatically shifting the mix of investments away from equities and towards bonds and cash as retirement nears (see chart 2).

Despite all the activity, experts caution against putting too much faith in financial education. "This is not the silver bullet that some people think it is," says Ms Smith. No campaign can hope to reach everyone. In addition, although those with more knowledge of finance tend to save more and make higher returns on their long-term investments, the strength of the effect is not clear.


A matter of life and life
2
Lifestyle and life-cycle fund assets* in the United States, $bn
Other investors
Individual retirement accounts
Employer-sponsored defined-contribution plans
120
100
80
60
40
20
0
1996 97 98 99 2000 01 02 03 04
*A lifestyle mutual fund is a hybrid fund that maintains a predetermined risk level. A life-cycle fund is a hybrid fund that typically rebalances to an increasingly conservative portfolio as the target date approaches
Source: Investment Company Institute

Annamaria Lusardi, an economist at Dartmouth College, and Olivia Mitchell, of the University of Pennsylvania's Wharton School, have found that few employees attend financial seminars even when they are offered in the workplace. Scepticism about hidden sales pitches and slanted advice abounds, particularly in the wake of recent mutual-fund scandals. "Workers are entitled to believe this is not an objective voice," says Ms Lusardi. Many who attend do not absorb what they hear, for want of understanding or interest.

In Europe they seem to be just as sceptical. In a report published this week, Forrester Research, a consulting firm, said that only one-third of Europeans trusted financial institutions to treat them fairly, and less than half trust the advice they get from their main bank. Only 20% think the information in promotional material will help them improve their financial decision-making.

Well-aimed information can make a difference, though. In Sweden, which started a new pension system in 1999, a

mixture of financial education and a media campaign prompted more people to choose their mix of investment funds for themselves. The effect faded when the information programme was discontinued.

Some dismiss worries about low financial literacy. “Complaints that people are too stupid to manage their own money are dead wrong,” wrote James Glassman, a fellow at the American Enterprise Institute, recently. He points, for example, to America's record levels of home-ownership.

There is good reason to believe that people will learn if they want to and if they must. It is not so long since the go-go 1990s, when millions started investing for the first time. Many then learned painful lessons about the risks of overenthusiasm for equities. Perhaps a strong message is needed to get people saving now for retirement a few decades away. Ms Lusardi offers a suggestion: “Tell them, ‘you're going to be poor, it's going to be tough'. The mutual-fund companies show pictures of cruises. You've got to show a nursing home and they'll give it some thought. Tell them poverty at retirement is hell.”

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The corporate-pension shift

Join the queue

Jan 12th 2006
From The Economist print edition

More companies move towards defined-contribution pension plans

THE sale of its personal-computer business to the Chinese was more striking, but not much. IBM's decision last week to restructure its American pension plans will have been noted by chief financial officers everywhere. A giant known for the generosity of its benefits said it will halt its defined-benefit pension plan and will set up a new 401 (k) scheme putting employees in control of their own retirement savings.

Americans have become accustomed to stricken airlines and steel companies giving up on their pension plans. But now a growing number of healthy firms like Big Blue are freezing their traditional pension schemes and shifting risks and more of the financing burden on to workers. Motorola and Verizon have made similar decisions.

The Employee Benefit Research Institute, a group supported by unions and corporations, reports that defined-benefit plans peaked in the 1970s but fell sharply over the next two decades. Meanwhile, defined-contribution schemes have risen steadily, covering 62% of workers by 2004.

In Britain, where companies are also finding defined-benefit schemes burdensome, there has been a similar trend. A 2005 study by Watson Wyatt, a consultancy, showed that 78 of the country's 100 largest public companies offer defined-contribution plans. Some also have defined-benefit schemes, though increasing numbers of these are closed to new members. Only 21 offer defined benefits alone. The shift has occurred over a decade, as companies have tried to rein in pension costs. Gary Smith, of Watson Wyatt, recalls “the domino effect” that rolled through industries, including drugmakers and retail banks.

After a pause, the past couple of years have seen a new wave of defined-contribution plans. Mr Smith says this has been the product largely of changes in the regulatory environment and accounting standards, prompting companies to review their pension schemes.

This week the union representing British Airways' pilots said its members might strike over proposed changes to pensions. And last month Rentokil, a services conglomerate, became the first member of the FTSE 100 index to say it wanted to close its defined-benefits plan to further accruals from members. More changes—and rows—are expected.

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American banks and property

Sleeping in the vault

Jan 12th 2006 | NEW YORK
From The Economist print edition

A move into hotels blurs the distinction between banking and commerce

TWO middle-sized American cities, Pittsburgh, Pennsylvania and Charlotte, North Carolina, will each see the rise of new hotels. Whatever significance this has for the cities themselves (and it may be noteworthy, at least for Pittsburgh) it has more for America's financial system. The owners will include two big banks, PNC (once known as Pittsburgh National Bank) and Bank of America (*née* North Carolina National Bank). The projects, approved last month by the Comptroller of the Currency, a national bank regulator, seemingly fly in the face of restrictions on investment in property dating back to the charter written in 1791 for the First Bank of the United States by Alexander Hamilton, America's first treasury secretary.

Hamilton's concerns were hardly unique. They were shared by, among others, Walter Bagehot, editor of this newspaper from 1861 to 1877, and have not been extinguished to this day. Loans and other financial assets, after all, can be blended with other loans and assets to permit diversification. They can usually be sold on fairly easily, either in bits or their entirety. And even “long-term” loans, at least those held by banks, tend to last for only a few years.

Conversely, property comes in lumps and can be hard to unload in a slump. Because American banks can raise money cheaply through federally insured deposits, there has always been a concern that by directly owning any kind of business, they could help inflate a bubble. That, along with the justified concern that crippled banks can trigger systemic problems, has resulted in limits being placed on their permissible activities. Even as, in recent years, lines have softened between banking, investment banking and insurance, general commerce has largely been off limits.

In response to these reservations, both PNC and Bank of America note that the restrictions have never been absolute. Banks have owned their branches and operational facilities, and prevailed in litigation permitting them to rent out surplus space and receive property pledged as collateral after a default. If this were not so, banking would be a vastly more complex business. Certainly, mortgages could not carry lower interest rates than other bank loans nor have developed as they did without the ability to use property as collateral.

To buttress its decision, the Comptroller's office referred to a 1902 Federal Appeals Court decision. The court held that banks would never find suitable places in crowded downtown business districts unless they could have the right to rent out surplus space acquired in a good-faith effort to house their operations. Going a bit further, the Comptroller's office released two previously undisclosed letters from 1993, the first acceding to a bank's request to hold a condominium for its own use and the second allowing the bank to rent it out when it was not needed.

Each of these steps was innocuous. PNC and Bank of America argue that their projects are similarly mere augmentations of their existing operations. PNC will build a $170m hotel-office-condominium project on a derelict site next to its headquarters. Perhaps it could be considered part of those headquarters. Local officials could not be more thrilled. Pittsburgh's mayor and Pennsylvania's governor joined the bank's chief executive to announce the project, and various city and state funds will pick up 30% of the cost. PNC's financial commitment will not, however, be reflected in its occupancy of the new structure. Almost half of the office space will be used by Reed Smith, a law firm. PNC says it will use “some” of the rest.

Bank of America's project goes one step further—across the street rather than next door. It is putting up a $60m hotel, one of the swanky Ritz-Carlton chain, with 150 rooms. Critical to the approval by the Comptroller was a pledge that half the rooms would be used by its own employees, thus making the project a bit less like a property speculation and more like the routine addition of a facility. That said, monitoring hotel occupancy is not an activity that bank regulators routinely undertake. Bank of America will, indirectly, be in the property-management business. Given the bank's vast array of offices around the country, might other property schemes be on the

drawing board? Surely other banks are looking around too. According to the *Charlotte Observer*, Wachovia, Bank of America's perpetual rival, hopes to build an office-condominium-arts facility. It would be a surprise were other moves long in coming.

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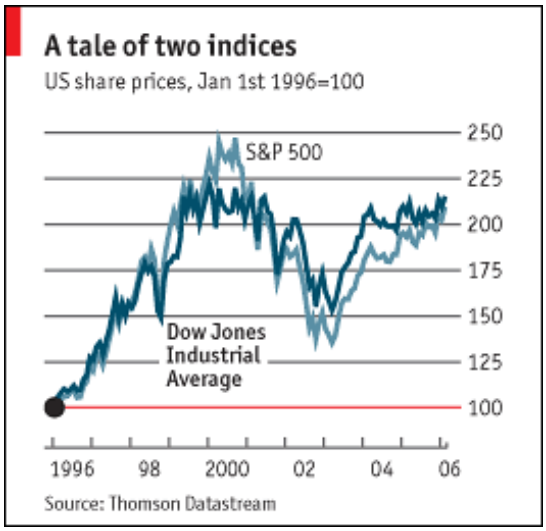
Stockmarket indices

The Dow puffs on

Jan 12th 2006
From The Economist print edition



America's most famous stockmarket index is also its most peculiar

SINCE the height of the railroad age, the Dow Jones Industrial Average has tracked the fortunes of a select group of America's corporate leviathans. Many in the markets think the Dow is no more modern than a steam locomotive. But the index still holds some resonance. Witness the ballyhoo on January 9th when it closed above 11,000 for the first time since June 2001, although it was still 6% below its all-time high.

Lots of people watch the Dow. Some also bet money on it. The Diamonds Trust, an exchange-traded fund, lets investors buy the index, more or less. The trust provided a meagre pre-tax return of 1.53% in 2005.

Most fund managers, though, judge themselves against the S&P 500 index, which returned a few percentage points more than the Dow last year, but is still 15% below its peak.

The Dow is an anachronism. Despite its name, it is no longer wholly industrial (J.P. Morgan Chase has never made a widget) but it does still resemble an average. Charles Dow, its inventor, first published his index in 1896 by simply adding up the price of 12 stocks and dividing by 12. The calculation is now a little more sophisticated—it takes some account of stock splits, big dividend payouts, and the reshuffling of its pack, now of 30 companies—but it still bears the influence of Charles Dow's finger-exercise. The companies with the highest share price, not the biggest market capitalisation, still carry the most weight. As a result, Alcoa counts for more than Microsoft, a company ten times as large.

Much has been made of this flaw, but it makes surprisingly little difference in practice. In 2000 John Shoven and Clemens Sialm of Stanford University redid the Dow, weighting each company by its market heft. The real Dow became a 30-strong index in October 1928 at 239.43 points and ended 1999 at 11,497. From the same starting position, Mr Shoven's and Mr Sialm's version reached 12,212. Their Dow outperformed its cruder cousin in 429 out of 855 months and underperformed in 426.

However the Dow stacks its blue chips, there are simply too few of them on the board. Thirty companies is too small a number to diversify away the idiosyncratic risks associated with each one. The Dow's triumph this week was actually a reflection of this handicap. General Motors, the ailing carmaker, enjoyed a rare good day—a Goldman Sachs report suggested that the company is not quite as sick as everyone assumed. And because GM

accounts for 1.6% of the Dow, compared with 0.12% of the S&P 500, the Dow is sharing more of the carmaker's highs and lows than it needs to.

The Dow is notoriously slow to shuffle its pack. This conservatism has little economic rationale. Industrial change does not respect past pedigree, otherwise National Lead and Distilling & Cattle Feeding, two of the original 12 stocks, would still be proud members.

And yet the alternatives have their imperfections too. The S&P 500's members are shuffled more often, and according to so many criteria, that some money movers complain they are batting against something resembling an actively traded fund, not a passive index. In particular, in its quest to remain representative of the American stockmarket, the S&P 500 will admit companies riding high on a wave of irrational exuberance, which pushes newly promoted stocks still higher. Philip Cusick, of Bear Stearns, has found that companies invited into the index enjoy an abnormal jump in the price of their stock, which averages 4.34% between the day their inclusion is announced and the end of the next trading day.

So is the Dow a relic? It rides on a narrower gauge than its newer rivals. But it is not yet bound for the scrapyard.

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Economist.com FINANCE & ECONOMICS

Credit cards

Making advances

Jan 12th 2006 | HONG KONG, LONDON AND MUMBAI
From The Economist print edition

Credit-card companies are eager to issue plastic in developing countries. But making money there might not be easy

THE amount that some people in rich countries borrow on credit cards is causing consternation to many consumer groups and debt counsellors. Now the cards are becoming increasingly common in developing countries too. And card-holders in China, Brazil and other emerging markets could teach their more affluent counterparts a thing or two about managing debt. They appear to be reluctant to borrow on cards for long and hence to pay much in interest. As a result, lenders are so far finding profits hard to come by.

America's General Electric, a giant of consumer finance, has issued 68m cards worldwide. Some 40% of those are in the hands of citizens of developing countries. In India 14m cards have been distributed by banks, including Citigroup and Standard Chartered, over the past decade and that number is growing by 25-30% a year, even though Indians use credit cards mostly for pricey items, such as air fares, and seldom for everyday purchases.

The aim for financial institutions is simple: to find new revenues as growth in some rich countries slows: the average American, for instance, already has eight cards. The potential seems enormous. In Brazil, Russia and India, spending on cards as a proportion of GDP is less than one-fifth of that in Britain.

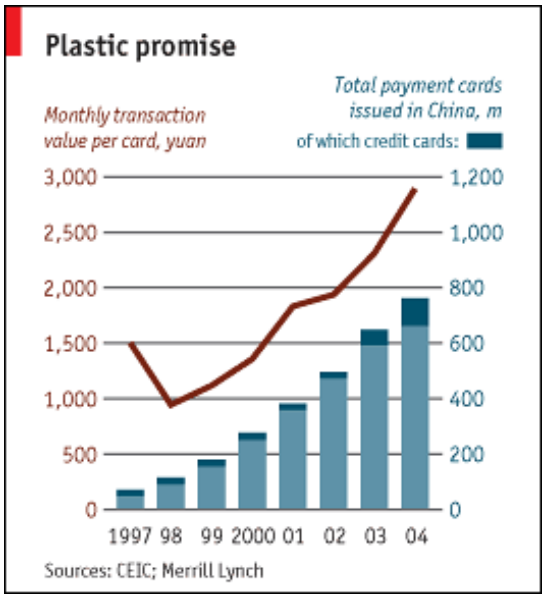
Other organisations, such as the Netherlands Development Finance Company (FMO), a development bank partly owned by the Dutch government, see credit cards less as a way of making money than as a form of “financial emancipation” for people who have never had contact with the formal economy. Last October FMO financed a programme that distributed credit cards to low-income households in El Salvador and Panama, with interest rates of 20-40%. One credit-card programme begun by another organisation in Mexico in August 2004 issued 250,000 cards in its first 14 months. Another 20,000 have been issued each month since, according to FMO.

The volume of credit-card transactions in developing economies is certainly growing fast—by 20-40% each year, according to Mercer Oliver Wyman, a consultancy—but few customers pay much interest on their debt, preferring instead to settle it as quickly as possible. The number of credit cards in Brazil, for instance, grew, on average, by 17.3% a year between 1999 and 2004, says Bain & Company, another consultancy. Brazilians, however, tend to pay off their monthly bills, partly because interest rates are high (8-11% a month) but also because they prefer to use cards as a convenient means of payment rather than as a way to borrow. There are other, cheaper loans available, says Rodolfo Spielmann of Bain. This may explain why Brazilians' annual spending on credit cards fell by 4.1% a year, in inflation-adjusted terms, between 1999 and 2004.

Like almost all international companies, credit-card issuers see China as a vast potential market, and the number of cards in circulation is growing at a cracking pace (see chart). Most local lenders have launched a card in the past couple of years, many of them in joint-ventures with foreign banks that understand the risks better. BoCom, the fifth-largest domestic lender in China, is undertaking a venture with its partner, HSBC, for instance. Although credit (as opposed to debit) cards make up only a small share of all the bank cards in China, consultants at McKinsey foresee rapid growth—and predict profits of $1.6 billion by 2013.

However, whether and when anyone in China will make good money from this business is not yet clear. McKinsey estimates that half the existing accounts are unprofitable. One reason is that Chinese customers have little brand loyalty, are not impressed by foreign-backed offerings and frequently switch providers. According to Bain, only 4-5% of

customers pay interest frequently. Some 85% pay their account balance in full every month, compared with 40-50% in richer economies.



Acquiring customers is also already at least as expensive as in developed countries, while spending levels are far lower. Ron Logan, head of HSBC's credit-card venture with BoCom, says that as competition heats up, acquisition costs are soaring, with everything from DVD players and holidays being used to entice customers. Jean-Jacques Santini of BNP Paribas, which recently bought a fifth of Nanjing City Bank, warns those venturing into the market: “Expect to lose money on credit cards for the first three or four years.”

Elsewhere, the story is similar. Card issuers in developing countries often depend for their revenue on the fees (1% or so of the transaction value) collected from merchants. This is enough to get by, but not to generate much of a profit.

Perhaps card-holders' discipline will waver as plastic is used to pay for a broader range of goods and services, and as more payment technology is installed in local businesses. Indian authorities are already worried about mounting debt. In November the central bank tried to rein in marketing by issuers after complaints that cards were being foisted on customers who could not afford debt. South Koreans have shown that accidents can happen when credit is easy. A credit-card spending spree, fuelled by tax incentives, earlier this decade brought some of the country's banks to the verge of collapse. Bad borrowing habits are not, after all, the preserve of Americans and Britons.

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Relative economic performance

Les misérables

Jan 12th 2006
From The Economist print edition

The misery index celebrates its 30th birthday. Time for a revamp?

IS THE economy in a better or worse state than ten years ago? The “misery index” (the sum of unemployment and inflation rates) is a back-of-the-envelope gauge of economic health. The higher the score, the greater the economic misery. It was invented by Arthur Okun, an American economist, just after the first oil crisis of the 1970s caused a sharp rise in both unemployment and inflation. Jimmy Carter popularised the misery index during his successful presidential campaign in 1976.

The classic misery index makes America's economy look pretty good, compared both with the past few decades and with much of Europe, burdened by higher jobless rates. But like many people when they hit 30, the index may be due for a spruce-up.

Merrill Lynch's economists have come up with a broader, international index. In addition to unemployment and inflation, it also adds interest rates and the budget and current-account balances, but then subtracts GDP growth (a good thing). In other words, the index not only reflects how cheery an economy feels today, but, by including budget and external balances, it also captures the ability of a country to sustain its merriment. For example, a large budget deficit probably implies higher taxes in future.

This new index could wipe the smile off the faces of exuberant Americans. The United States has the highest score (see chart), ie, it has the most wretched economy among the big G7 countries, thanks to its huge deficits. In the 1990s, by contrast, before its imbalances exploded, its index was one of the lowest. The United States is the only country to have seen a large increase in its misery index over the past decade. Virtually all the other G7 countries—including Europe—have seen sizeable improvements.

Japan, after a decade of woe, is now back to where it was in 1994. However, Japan's misery index is somewhat misleading, since, in effect, it treats deflation as good, not bad.

The superstar that deserves to smile is Canada. Over the past decade it has seen the biggest reduction in its misery index of any G7 economy. It is the only country running both current-account and budget surpluses—in happy contrast to its southern neighbour.

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Economics focus

The aggro of the agora

Jan 12th 2006
From The Economist print edition

Consumers fail to measure up to economists' expectations

"WE MUST accept the consumer as the final judge," wrote Frank Taussig, a former president of the American Economic Association (AEA), in 1912. His view was once an article of faith of the economics profession: the consumer was sovereign, the market his servant. It fell to economists only to explain the consumer's decisions, not to second-guess them.

The AEA's latest annual meeting, held last weekend, made one thing abundantly clear: this ritual deference to consumer sovereignty is slipping. Among the opening sessions was one entitled "The economics of paying too much", a rich genre that spans gym memberships, banking fees and inkjet cartridges. The next day, John Campbell, president of the American Finance Association (AFA), dwelt on the failure of households to hold enough shares, diversify their assets fully or refinance their mortgages promptly. Meanwhile, Daniel McFadden, the AEA president, argued that the unshackling of markets, which has proceeded apace since the 1980s, would fall short of its promise if consumers were not similarly freed from the fetters of ignorance, self-deception and intemperance.

Mr McFadden's speech leaned on the work of neuroeconomists, who claim to prove what Adam Smith long ago asserted: man's "propensity to truck, barter and exchange" runs deep in our nature. According to brain scans, it lurks in the same primitive, limbic vaults of the cerebrum as our instinct to fight, flee and feed ourselves. Indeed, "shopping and sex share the same neurotransmitters and receptors," Mr McFadden jokes.

But if trading turns some people on, it puts others off. Markets can be "rough, murky, tumultuous places". Consumers may doubt themselves, the products on display and the people flogging them. Losing out—paying too much—is an ever-present danger. This can be character-building, of course. By punishing a consumer's mistakes and inconsistencies, the market may whip him into shape, so that he more closely resembles the rational actor an efficient market deserves. But Mr McFadden worries that consumers may instead develop an aversion to markets: "Opportunities for choice may be interpreted as opportunities for mistakes, embarrassment and regret." He calls this agoraphobia. In common parlance, this is a fear of open spaces; translated literally from Greek, it means "fear of the marketplace".

In his class at the University of California, Berkeley, Mr McFadden randomly handed out pencils, embossed with the course's name, to half of his 345 students. He then held a sealed-bid auction, designed so that no one had any reason to lie about how much a pencil was worth to them. Since the pencils were distributed at random, there was no reason to think pencil-owners should be any more eager to hold on to their pencils than bidders were to buy them. Whatever value the median student places on a pencil, about half the pencil-holders should value them less, and half of those without pencils should value them more. Thus 86 pencils should change hands.

In fact, only 32 pencils were traded. This might be the result of what economists call the "endowment effect": we value what we own more highly, simply because we own it. But Mr McFadden reckons that another explanation is also at work. Even for something as trivial as a pencil, fear of overpaying or selling too cheaply inhibits trade: "Consumers find trade an edgy experience...and resist trading for small gains."

This reluctance to face the market may also apply to much weightier matters. Listening to Mr Campbell's AFA address, it is easy to conclude that agoraphobia reigns over the American housing market. Most American mortgages offer fixed interest rates, but can be refinanced without penalty should the household so wish. The steep decline in interest rates between 2001 and 2003 prompted many households to do just that. But a large fraction fell victim to inertia. In 2003, Mr Campbell estimates, most households were still paying interest at more than a percentage point above the market rate; an eighth were paying a spread of more than three points.

Financial flossing

What to do? Mr Campbell is inspired by the example of dentistry. The big gains in oral health, he points out, stemmed from straightforward advice and easy-to-use products. Economists should promote the financial equivalent of brushing twice daily with toothpaste. Such simple, effective ideas are surprisingly rare in an otherwise competitive financial industry. Why, for example, does a mortgage lender not offer a fixed-rate mortgage that refinances automatically whenever the market rate falls too far below the rate the customer is paying?

Mr Campbell speculates that the agoraphiles profit at the expense of agoraphobes. Those households that do refinance their mortgage enjoy a better rate precisely because the remainder do not. As a consequence, lenders who wanted to introduce a self-refinancing mortgage would face a conundrum. Naive householders would benefit from such a product, but if they knew that, they would no longer be naive (and would not need it).

Mr McFadden takes all this a step further. The “consumer may need to be coaxed and wheedled into responding to market choices with sufficient diligence,” he says. For his predecessors, such as Taussig, this is heresy. The consumers' choices are the data—the given things—of economics. It is only by observing a consumer's choices that economists can infer his preferences. Thus to argue that we know what's best for consumers, independent of what they have chosen for themselves, is a failure of logic as well as the height of presumption. If our theory fails to explain their behaviour, it is our problem, not theirs. Mr McFadden seems tempted by the opposite conclusion. If economic theory fails to reflect consumer behaviour, perhaps consumers can be remoulded, better to serve the theory.

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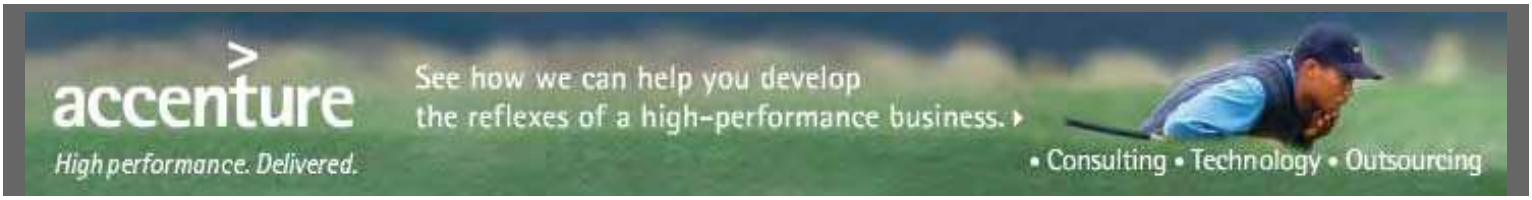
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Astronomy

Postcards from the edge

Jan 12th 2006
From The Economist print edition

A greater understanding of the Kuiper belt will fuel uncertainty over what, exactly, a planet is

Get article background

ONCE upon a time, people thought that the solar system consisted of four small, rocky inner planets, four large, gassy outer planets and an odd little runt called Pluto. Since the early 1990s, though, almost a thousand other runts have been discovered in the region of the solar system called the Kuiper belt, where Pluto resides. Most of these objects are a lot smaller than Pluto, but a few are of similar size and one called 2003 UB_{313} is larger.

Such discoveries have re-ignited a debate over whether Pluto should, indeed, be called a planet. More importantly, they are causing views of the outer solar system to evolve rapidly. The emerging picture of the Kuiper belt is that, far from being an obscure and peripheral feature, it is the largest structure in the solar system. The latest estimate is that it may contain 100,000 objects that have diameters of 100km (about 60 miles) or more.

That knowledge, though, has been won with telescopes. What astronomers would really like is a close-up look at Pluto and its neighbours. And that is what they should get with the launch of *New Horizons*, a probe put together by NASA, America's space agency. Unfortunately, they will have to wait until the middle of 2015 for the pictures to arrive.

Even that distant arrival date depends on things happening correctly over the next few weeks. *New Horizons* needs to take off between January 17th and February 14th in order to make use of gravitational assistance from Jupiter to speed it on its way. Should this launch window be missed, its arrival will be delayed by several years.

A visit to Hades

The craft itself is equipped with a variety of instruments intended to find out what Pluto and its largest moon Charon are made of. There is also a telescopic camera which will take the first decent pictures of Pluto, providing

enough detail to detect surface erosion and cratering.

And there is a lot to find out. What is known about Pluto thus far, said one NASA employee recently, “could basically fit on a postcard”. Its surface is known to include frozen nitrogen, carbon monoxide, methane and water, while the tenuous atmosphere is made mostly of nitrogen—but that's about it.

The Kuiper belt is also the source of material for a NASA mission that is coming to its end just before *New Horizons* takes off. *Stardust* has collected samples from a comet called Wild 2, which is believed to be a Kuiper-belt object that has wandered into the inner solar system. *Stardust* crossed Wild 2's path two years ago and is due to send its sample capsule back to Earth on January 15th. The capsule will enter the Earth's atmosphere at 46,000kph—the fastest re-entry ever made. The plan is that it will parachute into Utah.

While planets such as Pluto are likely to have been altered by weathering and geological processes since they formed 4.5 billion years ago, comets such as Wild 2 are thought not to have changed since they were created in the outer regions of the solar system. Like tiny frozen time machines, they offer a window into a past when the solar system was just forming.

After *New Horizons* has had its close encounter with Pluto, the plan is to send it to take a look at one or two other Kuiper-belt objects. There will be plenty to choose from. In the years between now and the probe's arrival it is likely that tens of thousands of new ones will have been seen by the world's telescopes.

These other Kuiper-belt objects should be as intriguing as Pluto itself, according to Alan Stern, of the Southwest Research Institute, in Boulder, Colorado, who is the chief scientist on the *New Horizons* mission. He says that ice-dwarfs such as Pluto are like planetary embryos. They are, however, embryos that were stunted and never grew large enough to reach the size of Earth. Nobody understands why their growth was interrupted, but it is hoped that *New Horizons* will reveal more. Understanding these objects, says Dr Stern, is fundamental to understanding the architecture and origin of the solar system.

While Pluto is large for a Kuiper-belt object—it has a diameter of 2,300km—its mass is less than 1% of Earth's. This and the presence of other similar-sized or larger things in the belt are fuelling a debate about what should count as a planet. Dr Stern argues that Pluto is a genuine planet, because it is rounded by the force of its own gravity. As he puts it, “it's a dwarf planet by the same measure a Chihuahua is still a dog.”

In that case, though, 2003 UB_{313} should also be called a planet. But nobody can agree on this, so last year the International Astronomical Union (IAU) convened a group of senior astronomers to suggest a new definition of what it is to be a planet.

What's in a name?

You might think that would be simple. But even though the committee has now presented its report, Kenneth Pounds, vice-president of the IAU and an astronomer at the University of Leicester, in England, says that the planet question remains in “some state of confusion”. Iwan Williams, an astronomer at the University of London who was asked to chair the IAU planet-definition group, explains that his task turned out to be a difficult one. The only thing the group managed to agree on unanimously was the fundamental difference between those objects that are made spherical by their own gravity and those, such as asteroids and comets, that remain lumpy. The problem with this definition, says Dr Williams, is that it produces “far too many planets”—meaning 30, including many of the solar system's larger moons.

Another possibility the IAU group discussed was whether a planet should be defined as something that is “dominant in its own neighbourhood”. Yet according to this definition, Pluto would not count as a planet, because it is only one of many similar objects in the region.

Such a definition would lead to several problems. For one thing, astronomers working on Pluto do not want a demotion. For another, the last time the IAU considered reclassifying Pluto as something other than a planet, it caused a public outcry. Then there is the question of what to call Pluto if it were demoted. For example, the term “minor planet” is today applied to asteroids, but, by any definition, most asteroids are not planets.

By a tiny majority, the IAU group voted that the best option was some kind of arbitrary size-distinction. Dr Williams says that a radius of 1,000km seemed sensible because, “100km is silly and 10,000km would not include Earth”.

The debate is not over yet, however. The final decision will be taken at the IAU general assembly in Prague this August, where astronomers will have the job of trying to balance the scientifically useful with the culturally

acceptable. If they can agree on the matter, then 2003 UB{-3}{-1}{-3} will finally get a proper moniker. If it is deemed to be just another miserable lump of rock and ice a very long way away, its discoverer, Michael Brown of the California Institute of Technology, will be allowed to give it a name. But if it is classified as a planet, then it will acquire a suitably grand name belonging to one of the classical gods.

That, however, would probably be just the start. If anything round and larger than 1,000km in radius is decreed a planet, then the Kuiper belt could contain a lot more of them. When Gustav Holst composed the “Planets” suite, Pluto had yet to be discovered. If he were alive today, he might have plenty of extra movements to write.

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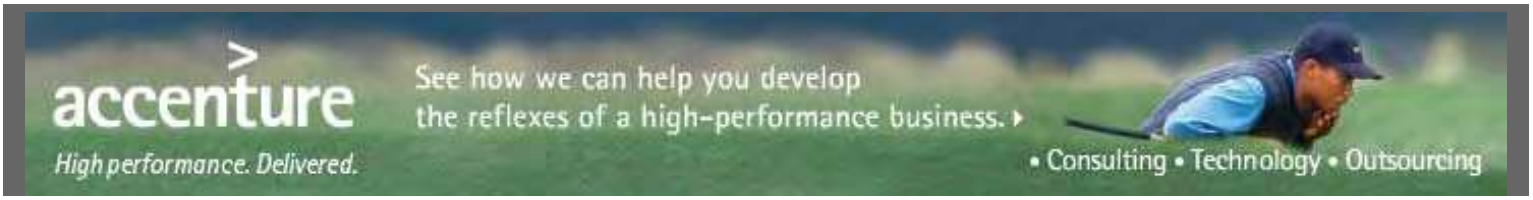
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Dog days for Dr Hwang

The Korean cloning scandal

Jan 12th 2006
From The Economist print edition

Get article background

AP

Yet more humiliation for Hwang Woo-suk. Last month, Dr Hwang was found to have made up claims, published in 2005, that he had cloned 11 people and derived lines of stem cells from the resulting embryos. Stem cells are the source of the specialised cells that make up the body, and the participants in the study were suffering from the sorts of disease (for example, diabetes) which it is hoped that such cells might one day cure. On January 10th an investigating team from Dr Hwang's former employer, Seoul National University in South Korea, announced that his original claim, made in 2004, to have cloned a human embryo and derived stem cells from it was also false. Dr Hwang's only crumb of comfort was that the panel believed his claim to have cloned a dog, nicknamed Snuppy (Seoul National University Puppy). *Science*, the journal that published the two human-cloning papers, is now retracting them. Meanwhile its rival *Nature*, which published the dog paper, is trying not to look too smug.

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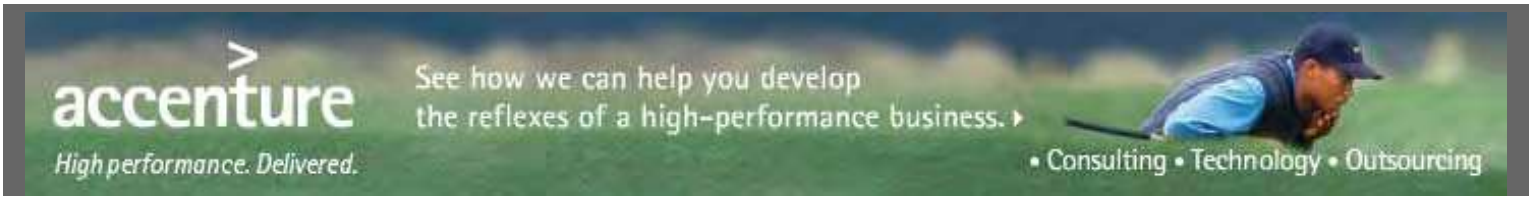
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Evolution and conservation

The law of unintended consequences

Jan 12th 2006
From The Economist print edition

A conservation project in New Zealand has inadvertently tested a piece of evolutionary theory

THE kakapo is widely regarded as the world's most absurd bird. It is a flightless, nocturnal parrot that lives in New Zealand. It is thus a prime example of the sort of evolutionary experiment that happens on islands that lack serious predators—or, rather, that lacked them until the arrival of mankind and his feline and canine hangers-on.

Now, sadly, the kakapo population has been reduced to a few dozen individuals confined to predator-free islets. But efforts to preserve the species have inadvertently led to another sort of evolutionary experiment—one that has produced the best evidence so far for a branch of the field called sex-allocation theory.

Bruce Robertson, of the University of Canterbury, in Christchurch, and his colleagues, have been studying a mystery. To keep the kakapo population going, conservationists have been feeding the birds—in particular, the females—so that they stay above the minimum weight they need to breed. That worked splendidly as far as it went. Between 1997 and 2005 the adult population rose from 50 to 83. But the sex ratio went haywire. Those 83 birds are divided into 45 males and 38 females. Moreover, females were producing twice as many sons as daughters. Since another of the kakapo's peculiarities is its breeding system in which, uniquely for parrots, the male plays no part in raising the young, the survival prospects of the species are not enhanced by this biased sex ratio.

Dr Robertson suspected that the sex ratio was not an accident. In all species the number of descendants left by individual males is more variable than the number left by individual females. That means your daughters are more likely to have at least some children than your sons, but successful sons have many more children than successful daughters. In a species such as the kakapo, where the males have to display to the females in a fashion show known as a lek, and where only the showiest males get picked to reproduce, it makes sense to have sons only if they are likely to be the best males around. Otherwise it is better to have daughters.

And so it seems to be with the kakapo. By provisioning the birds with as much food as they can eat, females have been brought to the peak of condition—the ideal state to produce top-class sons. And they have done so, in abundance.

To test the correctness of this idea, and also to improve the kakapo's prospects, Dr Robertson and his team devised a more sophisticated feeding schedule that took account of each female's starting weight and fattened her up to the point at which she was capable of reproducing, but not much further. The result, just published in *Biology Letters*, was that the sex ratio settled down at a more sensible 50:50. Though it did not actually drop to favour daughters, that is still an impressive agreement with theory. It might even save the kakapo from extinction.

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Chinese cartography

China beat Columbus to it, perhaps

Jan 12th 2006
From The Economist print edition

An ancient map that strongly suggests Chinese seamen were first round the world

THE brave seamen whose great voyages of exploration opened up the world are iconic figures in European history. Columbus found the New World in 1492; Dias discovered the Cape of Good Hope in 1488; and Magellan set off to circumnavigate the world in 1519. However, there is one difficulty with this confident assertion of European mastery: it may not be true.

It seems more likely that the world and all its continents were discovered by a Chinese admiral named Zheng He, whose fleets roamed the oceans between 1405 and 1435. His exploits, which are well documented in Chinese historical records, were written about in a book which appeared in China around 1418 called “The Marvellous Visions of the Star Raft”.

Next week, in Beijing and London, fresh and dramatic evidence is to be revealed to bolster Zheng He's case. It is a copy, made in 1763, of a map, dated 1418, which contains notes that substantially match the descriptions in the book. “It will revolutionise our thinking about 15th-century world history,” says Gunnar Thompson, a student of ancient maps and early explorers.

The map (shown above) will be unveiled in Beijing on January 16th and at the National Maritime Museum in Greenwich a day later. Six Chinese characters in the upper right-hand corner of the map say this is a “general chart of the integrated world”. In the lower left-hand corner is a note that says the chart was drawn by Mo Yi Tong, imitating a world chart made in 1418 which showed the barbarians paying tribute to the Ming emperor, Zhu Di. The copyist distinguishes what he took from the original from what he added himself.

The map was bought for about $500 from a small Shanghai dealer in 2001 by Liu Gang, one of the most eminent commercial lawyers in China, who collects maps and paintings. Mr Liu says he knew it was significant, but thought it might be a modern fake. He showed his acquisition to five experienced collectors, who agreed that the traces of vermin on the bamboo paper it is written on, and the de-pigmentation of ink and colours, indicated that the map was more than 100 years old.

Mr Liu was unsure of its meaning, and asked specialists in ancient Chinese history for their advice, but none, he says, was forthcoming. Then, last autumn, he read “1421: The Year China Discovered the World”, a book written in 2003 by Gavin Menzies, in which the author makes the controversial claim that Zheng He circumnavigated the world, discovering America on the way. Mr Menzies, who is a former submariner in the Royal Navy and a merchant banker, is an amateur historian and his theory met with little approval from professionals. But it struck a chord: his book became a bestseller and his 1421 website is very popular. In any event, his arguments convinced Mr Liu that his map was a relic of Zheng He's earlier voyages.

The detail on the copy of the map is remarkable. The outlines of Africa, Europe and the Americas are instantly recognisable. It shows the Nile with two sources. The north-west passage appears to be free of ice. But the inaccuracies, also, are glaring. California is shown as an island; the British Isles do not appear at all. The distance from the Red Sea to the Mediterranean is ten times greater than it ought to be. Australia is in the wrong place (though cartographers no longer doubt that Australia and New Zealand were discovered by Chinese seamen centuries before Captain Cook arrived on the scene).

The commentary on the map, which seems to have been drawn from the original, is written in clear Chinese characters which can still be easily read. Of the west coast of America, the map says: “The skin of the race in this area is black-red, and feathers are wrapped around their heads and waists.” Of the Australians, it reports: “The skin of the aborigine is also black. All of them are naked and wearing bone articles around their waists.”

But this remarkable precision, rather than the errors, is what critics of the Menzies theory are likely to use to question the authenticity of the 1418 map. Mr Menzies and his followers are naturally extremely keen to establish that the 1763 copy is not a forgery and that it faithfully represents the 1418 original. This would lend weighty support to their thesis: that China had indeed discovered America by (if not actually in) 1421. Mass spectrography analysis to date the copied map is under way at Waikato University in New Zealand, and the results will be announced in February. But even if affirmative, this analysis is of limited importance since it can do no more than date the copyist's paper and inks.

Five academic experts on ancient charts note that the 1418 map puts together information that was available piecemeal in China from earlier nautical maps, going back to the 13th century and Kublai Khan, who was no mean explorer himself. They believe it is authentic.

The map makes good estimates of the latitude and longitude of much of the world, and recognises that the earth is round. “The Chinese were almost certainly aware of longitude before Zheng He set sail,” says Robert Cribbs of California State University. They certainly assumed the world was round. “The format of the map is totally consistent with the level of knowledge that we should expect of royal Chinese geographers following the voyages of Zheng He,” says Mr Thompson.

Moreover, some of the errors in the 1418 map soon turned up in European maps, the most striking being California drawn as an island. The Portuguese are aware of a world map drawn before 1420 by a cartographer named Albertin di Virga, which showed Africa and the Americas. Since no Portuguese seamen had yet discovered those places, the most obvious source for the information seems to be European copies of Chinese maps.

But this is certainly not a unanimous view among the experts, with many of the fiercest critics in China itself. Wang Tai-Peng, a scholarly journalist in Vancouver who does not doubt that the Chinese explored the world early in the 15th century (he has written about a visit by Chinese ambassadors to Florence in 1433), doubts whether Zheng He's ships landed in North America. Mr Wang also claims that Zheng He's navigation maps were drawn in a totally different Chinese map-making tradition. “Until the 1418 map is scientifically authenticated, we still have to take it with a grain of salt,” he says.

Most forgeries are driven by a commercial imperative, especially when the market for ancient maps is booming, as it is now. The Library of Congress recently paid $10m for a copy of a 1507 world map by Martin Waldseemuller, a German cartographer. But Mr Liu says he is not a seller: “The map is part of my life,” he claims.

The consequences of the discovery of this map could be considerable. If it does indeed prove to be the first map of the world, “the history of New World discovery will have to be rewritten,” claims Mr Menzies. How much does this matter? Showing that the world was first explored by Chinese rather than European seamen would be a major piece of historical revisionism. But there is more to history than that. It is no less interesting that the Chinese, having discovered the extent of the world, did not exploit it, politically or commercially. After all, Columbus's discovery of America led to exploitation and then development by Europeans which, 500 years later, made the United States more powerful than China had ever been.

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American imperialism

Better with them than without them

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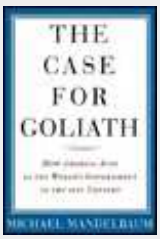
From The Economist print edition

America leads the world but does it rule it? And what should we feel about being part of the empire, if it is one?

The Case for Goliath: How America Acts as the World's Government in the 21st Century
By Michael Mandelbaum



PublicAffairs; 283 pages; $26 and £15.50

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AFP

Be careful before you wish them away

AS THE civilian death toll in Iraq continues to mount at an undiminished rate, as the prison scandals of Abu Ghraib and Guantánamo Bay continue to undermine any claim to a moral high ground, and as America continues to be a deliberate laggard in adjusting its energy policy to take account of global warming, it has become steadily harder to find non-Americans willing to agree that on balance American leadership makes the world a better place. That doesn't make the notion wrong, however. Enter Michael Mandelbaum, a foreign-policy expert at Johns Hopkins University in Washington, DC. His previous, very compelling book, “The Ideas that Conquered the World” (2002), explored how peace, democracy and free markets had become the world's dominant ideals. Now, his new book argues that the country that stands most squarely behind those aspirations, the United States, also acts as a sort

of surrogate government for the globe—and that we would all be a lot worse off if it didn't.

“The Case for Goliath” is somewhat less compelling than its predecessor, as it often reads like a rather ponderous textbook. But it is in a good cause and its arguments are well worth considering, especially given the recent trend of world opinion. As he argues, the right question to ask is not whether this or that act of American foreign policy could be improved upon, for many undoubtedly could be and should be. That has always been true, ever since the 1940s when America first took on a clear role as global leader. The better question is whether such American leadership—which he argues is a functional equivalent to being the world's government—is preferable to the plausible alternative. That alternative, in his view, consists of less governance not more, as neither a rival leader nor a collective solution is ready to fill the gap left by any American withdrawal. Be careful what you wish for, is in essence his message to those who go beyond criticising American actions to advocate their cessation.

Mr Mandelbaum does a fine service in showing why, in matters of peace and security, such anti-American views rest on a delusion. Without the American military to act as intervener of last resort, albeit at the head of NATO missions, the wars in the former Yugoslavia, the first on the European continent since 1945, simply would not have been brought to a halt. More generally, without the American presence and strength to act as a deterrent, war between the rising powers of Asia, for example, would look a lot more likely than it does. And without American steering and encouragement, the 50-year effort to limit nuclear proliferation would not have succeeded as well as it has.

Leading, not ruling

Where, however, he sows confusion amid his otherwise clear exposition is in his desire to replace the broad notion of “leadership” with the idea that America acts, in effect, as the world's government. Even in the military sphere, where America's lead over all others is at its greatest, this analogy is questionable. For real governments do not just act as interveners of last resort, as America did in the Balkans; they steer things much more actively. But the analogy becomes especially inapt in economic affairs. For in that sphere, America's efforts since 1945 can be seen as an attempt to ensure that no one needs to act as a world government. And those efforts have been strikingly successful.

Some critics of America look back on the 1940s, when President Harry Truman and his secretary of state, Dean Acheson, drove the establishment of the United Nations, its economic affiliates the IMF and the World Bank, and the separate General Agreement on Tariffs and Trade, as the high point of enlightened American leadership, designed to create a multilateral, rules-based world, in contrast to the brutish unilateralism of George Bush. Such claims ignore the fact that Messrs Truman and Acheson were eagerly unilateralist when they needed to be and that the initial hopes for the UN were stillborn. More important, though, they ignore the fact that in economics, finance and trade, the multilateral, rules-based world exists, and that America largely works within it.

To call the United States “the world's government” in economic affairs is plain wrong. It is more governed than governing, much to Congress's frequent discomfort. In the 20th century, to be sure, America played the decisive role in establishing all these rules, procedures and institutions. Contrary to Mr Mandelbaum's subtitle, however, in the 21st century all that can be said is that if the world's largest single economy were to withdraw from the World Trade Organisation, say, or the IMF, those institutions would collapse. It is indispensable but not in control. The same is true of the European Union. If the Doha round of WTO talks fails this year, it is as likely to be the EU's fault as America's. For in economics, the global trend since 1945, as more and more countries have adopted liberal forms of capitalism subject to common rules, has been towards greater equality both of wealth and of influence between the big countries and blocks.

The great irony of America's leadership of the world since 1945 has been that the more it succeeds in spreading its ideas—“conquering the world” with them, in Mr Mandelbaum's earlier words—the more that its economic pre-eminence becomes eroded. Among all the empires in history, if America deserves that word, it is as the first ever self-dissolving empire. Even Mr Bush, through his economic liberalism and his “freedom agenda”, would, if successful, eventually encourage multilateralism rather than challenge it.

Where Mr Mandelbaum is right is that in matters of peace and security, and in the technical work that lies behind those grand themes, the development of multilateralism is far less advanced—indeed in some ways it hasn't advanced at all. But there is only one thing worse than leadership from the White House and the Pentagon. And that is not having leadership from the White House and the Pentagon.

The Case for Goliath: How America Acts as the World's Government in the 21st Century.
By Michael Mandelbaum.
PublicAffairs; 283 pages; $26 and £15.50

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Happiness

A strangely newfangled idea

Jan 12th 2006
From The Economist print edition

IT WAS 1963 and the atmosphere at the State Mutual Life Assurance Company in Worcester, Massachusetts, was tense. Workers fretted about an approaching merger with another company. Who would stay and who would get the heave-ho? So the management commissioned an advertising man by the name of Harvey R. Ball to come up with something cheerful to smooth wrinkled brows and make the whole merger process a little more bearable for everyone.

Ball's brilliantly simple solution—a big yellow dot with a pair of black ovals for eyes and a wide semicircle for a mouth—went on to become one of the most distinctive icons of the 20th century. “Smiley face” buttons, T-shirts and bumper stickers were soon selling in their tens of millions all round the world. But was Ball smiling? Grinning through gritted teeth, more like. Never having filed trademark or copyright papers, he had to make do with his original fee of $45.

Happiness: A History
By Darrin M. McMahon

Atlantic Monthly Press; 544 pages; $27.50.

Buy it at
Amazon.com
Amazon.co.uk

This is just one of many ironies in Darrin McMahon's excellent history of happiness. His central argument is that the modern idea of happiness was an invention of the Enlightenment. The idea of heavenly felicity came down to earth, says Mr McMahon, during the 17th and 18th centuries. “Happiness, in the Enlightenment view”, he explains, “was less an ideal of godlike perfection than a self-evident truth, to be pursued and obtained in the here and now.” In 1776 America's Founding Fathers declared “the pursuit of happiness” to be one of man's “unalienable rights”, along with life and liberty.

Historically speaking, this was a radical change. For the ancient Greeks, happiness was largely bound up with notions of luck and fortune. Any man, however high and mighty, could be brought down by a twist of fate. The important thing, therefore, was not to seek happiness for its own sake but to live virtuously. Being good, as Mr McMahon nicely puts it, was more important than feeling good. For Herodotus and his contemporaries, happiness was not a “subjective state” but a “characterisation of an entire life that can be reckoned only at death.”

Later, Christianity would play down fortune and fate while holding out the promise of eternal happiness in the next life. With the Enlightenment, the idea that God was happiness morphed into the idea that happiness was god. By the 1840s the distinguished Scottish curmudgeon Thomas Carlyle was complaining: “Every pitifulest whipster that walks within a skin has had his head filled with the notion that he is, shall be, or by all human and divine laws ought to be, ‘happy'.” It is good that Carlyle did not live to see the self-help section of any big 21st-century bookshop, its shelves groaning with bestsellers like “Infinite Happiness”, “Absolute Happiness”, “Everlasting Happiness”, “Compulsory Happiness”, “Happiness Is Your Destiny” and “Find Happiness In Everything You Do”.

Carlyle was right to suspect that the new doctrine of happiness tended to raise unrealistic expectations, and his perception is still spot-on. Living standards and life expectancy are better than ever and a multi-billion-dollar pharmaceutical industry provides chemical solutions to gloomy moods. But are we really any happier now than we were in Carlyle's day—or, for that matter, in Herodotus's?

Mr McMahon sensibly does not try to define happiness and, in presenting the theories of great figures of the past, he does not take sides between them. He does, however, show particular sympathy for the views of John Stuart Mill. “Those only are happy”, Mill reckoned, “who have their minds fixed on some object other than their own happiness; on the happiness of others, on the improvement of mankind, even on some art or pursuit, followed not as a means, but as itself an ideal end. Aiming thus at something else, they find happiness by the way.”

Fair enough. But if Mill's suggestion that happiness is to be found “by the way” is a bit too hit-and-miss for your

liking, then you might try religion. Or sex. Or shopping. Or work. Or booze. Or Prozac. Or even sitting down with a good book.

Happiness: A History.
By Darrin M. McMahon.
Atlantic Monthly Press; 544 pages; $27.50.
To be published in Britain as "The Pursuit of Happiness: A History from the Greeks to the Present" by Penguin/Allen Lane in June

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New music

From the theatre of the synagogue

Jan 12th 2006 | NEW YORK
From The Economist print edition

A relaxed chance for New Yorkers to hear Osvaldo Golijov's music

A compositional globetrotter

A MUSICAL polyglot who embraces everything from klezmer to tango, Argentine-born Osvaldo Golijov is a composer with the rare ability to excite both critics and ordinary concertgoers. A fine example of this talent is his seminal work, “La Pasión Según San Marcos”, which sets the story of Jesus's crucifixion in contemporary Latin America. He invites his listeners to a jubilant Latin carnival, with blaring trumpets, hypnotic percussion, infectious samba and mambo rhythms. Along the way, ecstatic choruses, Gregorian chant and mournful Brazilian ballades wind towards the Kaddish, a fitting way for a Jewish composer to conclude a piece based on the Book of Mark.

This magnificent piece, which will be a highlight of the month-long festival to honour Mr Golijov that opens at Lincoln Centre in New York on January 22nd, was commissioned by Helmuth Rilling, a conductor, to commemorate the 250th anniversary of Bach's death in 2000. In less capable hands, a large-scale work featuring flamenco, tango, Yiddish melismas and Gregorian chant—using an eclectic range of performers from violinists to Cuban drummers—would be a disjointed, multicultural mishmash. In fact it works brilliantly. Composers often borrow from indigenous traditions, but Mr Golijov preserves disparate musical identities within a tight narrative framework. He explains that people want to hear a story, so, for example, he uses flamenco—the music of the Spanish conquistadors—to represent Jesus's betrayal.

Mr Golijov's other works are no less emotive. His hauntingly expressive string quartet “The Dreams and Prayers of Isaac the Blind” features a klezmer clarinet and strings that veer from eerie melancholy to Latin energy. His one-act opera “Ainadamar”, a Lincoln Centre co-commission that explores the life and work of Federico García Lorca, is also melodic. His string quartet “Yiddishbbuk”, his first major work, which he composed when he was 31 (he is now 45), is more dissonant.

He finds composing orchestral music difficult, because his music, which he describes as “semi-chaotic”, is at odds with orchestral hierarchies. “There isn't a conductor controlling everything. My music comes from the theatre of the synagogue, where one man mumbles, another screams.” Unusually for a musician, he is not inspired by nature, explaining that he “would rather meet a new person and examine him than a mountain.”

Mr Golijov wrote the songs on “Ayre”, his latest disc, for his muse, the soprano Dawn Upshaw. Traditional Jewish, Arab and Christian folk melodies and texts from 15th-century Spain are richly and eclectically scored for instruments that range from viola to laptop. The songs juxtapose themes of love, jealousy, religion, rage and war. The second song sets gruesome lyrics to a lovely, traditional melody with gentle string accompaniment. This melts into the introduction of the third song, which sounds, for a few seconds, like the work of an angry techno DJ.

This ambiguity is intentional. Mr Golijov says his music “is at its best when ambiguity is rich, not by avoiding emotions like modernist composers, but by affirming contradictory things like joy and sorrow.” He visualises while composing, and in the ominous, turbulent parts of the song “Wa Habibi” in “Ayre”, he imagined knives flying. “On television you see the seething anger of Arab streets, which for me is the equivalent of knives,” he says.

He is visibly frustrated when talking about modernist music. Music doesn't necessarily progress like science, he says. “Sometimes the arts get impoverished. It's not a secret what creates the impact of music. Harmony in western civilisation was the great mover from Bach onwards and a great melody can still transform you.”

Contemporary composers are often pigeonholed as modernist, minimalist or neo-romantic and write for a niche audience. Mr Golijov avoids this; his unusual ability to write music that is both visceral and intellectually stimulating attracted Lincoln Centre. He is also one of the few living composers awarded a recording contract with a major label. “Ayre” was his first release on Deutsche Grammophon.

Mr Golijov says that he “modulates cultures like other composers modulate keys.” He was born in La Plata, Argentina. His pianist mother's family were Romanian orthodox Jews; his music-loving physician father came from a family of atheist, socialist Russian Jews. He grew up listening to his mother practise Bach, singing in the local synagogue choir and enjoying Astor Piazzolla's tango. He studied the piano as a child, but ideas would pop into his head and he would compose instead.

At 23 he moved to Jerusalem for three years, where he absorbed Arab music. He went to the United States in 1986, and studied with George Crumb, an American composer. He now lives near Boston with his wife and three children. In person he is much like his music: passionate and outspoken, a gourmet who “loves the good life”. Wiry, dark-haired and gregarious, he speaks with his hands and laughs a lot.

He muses that if he could play Schubert or Mozart as well as he would like to do, perhaps he would not compose. But composition is his way to interpret the world, and he speaks to a broad audience. As he says, “I absorb, I distil and I put back. Music should speak to everyone.”

Several of Mr Golijov's compositions, including "Ayre", are to be performed at London's Barbican Hall on January 31st. A concert on February 24th will feature "La Pasión Según San Marcos".

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Yao Wenyuan

Jan 12th 2006
From The Economist print edition

Yao Wenyuan, the last of the Gang of Four, died on December 23rd, aged 74

AP

FROM the age of 15 Yao Wenyuan kept a diary, in preparation for writing his memoirs later. He knew his life might be important. At his trial in 1980, one particular entry was read out to him: “Why can't we shoot a few counter-revolutionary elements? After all, dictatorship is not like embroidering flowers.”

Of the awful quartet who unleashed and directed Mao Zedong's bloody Cultural Revolution, Mr Yao was the only one who had grand literary pretensions. Jiang Qing, Mao's fourth wife, wrote operas; Zhang Chunqiao was a political thinker; Wang Hongwen, an organising type, had been an official in a textile mill. Yet credit for China's descent into hell always went to Mr Yao and what was to become his most famous piece of writing: “On the New Historical Beijing Opera 'Hai Rui Dismissed from Office' ”.

The title hardly sang; and as seminal works go, this one, published in November 1965, was especially obscure. It was not even Mr Yao's idea; Madame Mao and Zhang had put him up to it. They knew that Chairman Mao was fascinated by the story of Hai Rui, a Ming dynasty official who had criticised the emperor to his face and had been sacked. A popular play about him, “Hai Rui Dismissed from Office” had been playing at the Beijing Opera for four years. But it was dangerously counter-revolutionary. Looked at through pure Maoist glasses, the emperor was Mao and Hai Rui was his defence minister, Peng Dehuai, who had been sacked in 1959 for openly criticising the Great Leap Forward, Mao's disastrous effort to collectivise industry and agriculture. Fearlessly, Hai Rui spoke up for the peasants:

> You pay lip service to the principle
> that the people are the roots of the state.
> But officials still oppress the masses
> while pretending to be virtuous men.
> They act wildly as tigers
> and deceive the emperor.
> If your conscience bothers you
> you know no peace by day or night.

If a counter-blast were needed to such subversive cant, Mr Yao's credentials were perfect. His base was Shanghai, a city that was friendlier to Mao in the early 1960s than Beijing was. He was the son of a left-wing writer from Zhejiang province, a leading light in Proletarian Writers for Purity and the editor of *Liberation Daily*, Shanghai's main newspaper. His history was solid orthodoxy. In the mid-1950s, when other angry young writers were beginning to edge away from China's communist revolution, Mr Yao had enthusiastically joined a state-run campaign to purge a famous writer, Hu Feng, from the writers' league for “subjectivism” and “self-reflection”—in other words, for thinking that idealistic individuals, as well as parties, could make revolutions. When more than 100 writers were brought down with Hu, many to be isolated in remote corners of China, Mr Yao exulted.

He fancied himself as Balzac to Mao's Napoleon, wielding his “golden” pen to smite the bourgeois individualists and “right deviationists” who might get in the chairman's way. When the Hai Rui business came up, he was happy to be useful. He took himself away to a sanatorium, pretending to be ill, in order to write his 10,000 words of diatribe against the play—words so tedious that the Beijing *People's Daily* published them as “Academic Research”. There were said to be ten drafts, three of which Mao wrote himself. The central thrust, however, was Mr Yao's: “If we do not clean up [this poison], it will harm the people's cause.”

It was nothing but a placeman's rant, but it unleashed the whirlwind. More articles followed, attacking public figures in the name of party purity. A Great Proletarian Cultural Revolution took shape, especially on university campuses, where students were recruited for a new “shock force”, the Red Guards. From January 1967 factories, banks and power plants were seized nationwide, while the Red Guards and the army sought out, terrorised or simply killed all deviants from orthodoxy.

What role Mr Yao played in all this is difficult to say. He was in charge of propaganda: so the hate-filled articles, the staged “free debates”, the “big-character” posters and banners and cartoons, may have had some origin with him. So may the use of Mao's quotations, handily bound in a little red book. But it seemed to some that Mr Yao was a puppet, not a master; that he went along happily, even sadistically, for the ride, and was swept up in the horror.

On Mao's death, in 1976, the Gang of Four's already waning primacy ended with arrest and disgrace. At his trial, Mr Yao was mostly silent, managing only to stutter that the words in his diary did not represent his views. He received the lightest sentence of the four, 20 years in Qincheng prison.

There he was glimpsed occasionally, a small, very bent figure in an all-grey Mao suit. He still kept his diary, and was said to be writing a book. So much self-reflection he could manage. China's rulers could not, and cannot. They had no interest in what he might write or say; after his release they allowed no one to speak to him, and even his death, announced two weeks late, was an embarrassment. China still has no way of coping with the trauma that Mr Yao's article helped unleash: one which Mao, a national hero, inspired, and in which millions joined.

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Overview

Jan 12th 2006
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Stockmarkets had a good week. On January 9th America's Dow Jones Industrial Average rose above 11,000 for the first time since June 2001. However, it is still 6% below its peak in January 2000. The S&P 500 is 15% below its peak. Stockmarkets in Sydney, Madrid, Toronto and Vienna, in contrast, all hit new highs during the week to January 11th.

America's unemployment rate fell to 4.9% in December. Only 108,000 new jobs were created in the month, around half the number that analysts had expected, but November's job growth was revised up sharply. Hourly wages rose by 3.1% from a year earlier, their fastest pace in almost three years. But wages are still rising more slowly than prices.

Business optimism in **Germany** continues to improve. The ZEW index of sentiment among analysts and institutional investors rose to 71, its highest since January 2004. Germany's trade surplus widened to $203.6 billion in the year to November.

Britain's trade deficit widened to a record £6 billion ($10.3 billion) in November, thanks to larger oil imports. The 12-month trade gap increased to $116.9 billion, up from $108.6 billion a year earlier.

Australia's monthly trade deficit almost doubled in November, because of soaring imports. However, the 12-month deficit narrowed to $15 billion.

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Output, demand and jobs

Jan 12th 2006
From The Economist print edition

% change on year ago

	GDP latest		GDP qtr*	The Economist poll GDP forecasts 2005	2006	Industrial production latest		Retail sales (volume) latest		Unemployment % rate latest		year ago
Australia	+ 2.6	Q3	+ 0.6	+ 2.7	+ 3.2	+ 0.7	Q2	+ 1.2	Q3	5.1	Dec	5.1
Austria	+ 1.8	Q3	+ 2.3	+ 1.8	+ 2.0	+ 3.0	Oct	+ 1.3	Oct	5.3	Dec	5.0
Belgium	+ 1.1	Q3	+ 1.7	+ 1.4	+ 1.9	– 7.7	Oct	+ 0.8	Oct	12.8	Nov†	12.8
Britain	+ 1.7	Q3	+ 1.7	+ 1.7	+ 2.1	– 2.4	Nov	+ 2.1	Nov	4.9	Oct††	4.7
Canada	+ 2.8	Q3	+ 3.6	+ 2.9	+ 3.1	+ 1.7	Oct	+ 2.2	Sep	6.5	Dec	7.0
Denmark	+ 4.8	Q3	+ 5.7	+ 3.0	+ 2.8	+ 4.6	Oct	+ 3.5	Nov	5.2	Nov	6.2
France	+ 1.8	Q3	+ 2.8	+ 1.5	+ 1.9	+ 1.3	Nov	+ 0.5	Nov	9.6	Nov	10.0
Germany	+ 1.4	Q3	+ 2.5	+ 1.1	+ 1.7	+ 4.7	Nov	– 0.6	Nov	11.2	Dec§	10.8
Italy	+ 0.1	Q3	+ 1.1	+ 0.2	+ 1.3	– 2.7	Oct	+ 0.4	Oct	7.7	Jun	8.1
Japan	+ 2.9	Q3	+ 1.0	+ 2.5	+ 2.4	+ 3.3	Nov	+ 0.4	Oct	4.6	Nov	4.6
Netherlands	+ 1.3	Q3	+ 2.5	+ 0.8	+ 1.9	+ 0.4	Nov	+ 3.5	Oct	6.5	Nov**	6.4
Spain	+ 3.5	Q3	+ 3.3	+ 3.4	+ 3.0	+ 0.8	Nov	+ 0.1	Nov	8.5	Nov	10.5
Sweden	+ 3.4	Q3	+ 3.9	+ 2.6	+ 3.1	+ 1.0	Nov	+ 9.0	Nov	5.0	Nov†	4.9
Switzerland	+ 2.3	Q3	+ 4.3	+ 1.8	+ 2.1	+ 2.8	Q3	+ 1.6	Sep	3.8	Dec†	4.0
United States	+ 3.6	Q3	+ 4.1	+ 3.6	+ 3.3	+ 2.8	Nov	+ 4.4	Nov	4.9	Dec	5.4
Euro area	+ 1.6	Q3	+ 2.6	+ 1.4	+ 1.9	+ 0.1	Oct	+ 0.3	Nov	8.3	Nov	8.8
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Finland	+ 1.9	Q3	+12.1	na	na	– 3.4	Nov	+ 5.6	Oct	8.3	Nov	8.7
Greece	+ 3.8	Q3	na	na	na	+ 0.9	Nov	+ 2.6	Oct	9.7	Q3	10.1
Iceland	+ 4.0	Q3	na	na	na	na		na		1.4	Oct†	2.7
Ireland	+ 4.8	Q3	+ 1.3	na	na	+14.8	Nov	+ 4.3	Oct	4.3	Dec	4.3
Luxembourg	+ 3.1	Q1	na	na	na	+ 4.9	Sep	– 2.9	Nov	4.9	Nov	4.4
New Zealand	+ 2.0	Q3	+ 0.2	na	na	– 1.5	Q2	+ 4.9	Q3	3.4	Q3	3.8
Norway	+ 3.1	Q3	+ 3.2	na	na	– 4.1	Oct	+ 3.8	Nov	4.6	Nov‡	4.5
Portugal	+ 0.2	Q3	– 3.7	na	na	+ 0.5	Nov	+ 1.1	Nov	7.7	Q3†	6.8

*% change on previous quarter at an annual rate. †Not seasonally adjusted. ††Aug-Oct; claimant count rate 2.9% in Nov. §EU harmonised rate 9.1% in Oct. **Sep-Nov.

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Don't let the information age

Prices and wages

Jan 12th 2006
From The Economist print edition

% change on year ago

	Consumer prices			The Economist poll consumer prices forecast		Producer prices			Wages/earnings		
	latest		year ago	2005	2006	latest		year ago	latest		year ago
Australia	+ 3.0	Q3	+ 2.3	+ 2.8	+ 2.9	+ 6.2	Q3	+ 6.1	+ 6.1	Q3	+ 3.5
Austria	+ 1.6	Nov	+ 2.6	+ 2.3	+ 1.9	+ 1.4	Dec	+ 5.2	+ 2.4	Nov	+ 2.0
Belgium	+ 2.9	Dec	+ 2.3	+ 2.5	+ 2.1	+ 1.7	Nov	+ 5.6	+ 2.3	Oct	+ 2.4
Britain	+ 2.1	Nov*	+ 1.5	+ 2.1	+ 2.0	+ 2.3	Nov	+ 3.5	+ 3.6	Oct†	+ 4.2
Canada	+ 2.0	Nov	+ 2.4	+ 2.3	+ 2.3	+ 2.9	Nov	+ 3.8	+ 2.8	Oct	+ 2.0
Denmark	+ 2.2	Dec	+ 1.2	+ 1.8	+ 1.9	+ 3.9	Nov	+ 3.2	+ 2.8	Q3	+ 2.9
France	+ 1.6	Nov	+ 2.0	+ 1.9	+ 1.7	+ 2.8	Nov	+ 3.2	+ 3.2	Q3	+ 2.9
Germany	+ 2.1	Dec	+ 2.1	+ 2.0	+ 1.7	+ 2.2	Nov	+ 4.1	+ 1.0	Oct	+ 2.3
Italy	+ 2.0	Dec	+ 2.0	+ 2.1	+ 2.1	+ 3.7	Nov	+ 4.3	+ 3.0	Nov	+ 2.7
Japan	– 0.8	Nov	+ 0.8	– 0.2	+ 0.3	+ 1.9	Nov	+ 2.1	– 0.3	Nov	+ 3.5
Netherlands	+ 2.0	Dec	+ 1.2	+ 1.5	+ 1.5	+ 4.5	Nov	+ 5.7	+ 1.1	Nov	+ 0.8
Spain	+ 3.4	Nov	+ 3.5	+ 3.4	+ 3.1	+ 4.9	Nov	+ 5.2	+ 1.9	Q3	+ 2.2
Sweden	+ 0.9	Dec	+ 0.5	+ 0.5	+ 1.5	+ 5.0	Nov	+ 2.9	+ 3.1	Oct	+ 3.8
Switzerland	+ 1.0	Dec	+ 1.3	+ 1.2	+ 1.1	+ 0.8	Nov	+ 1.9	+ 0.9	2004	+ 1.4
United States	+ 3.5	Nov	+ 3.5	+ 3.4	+ 2.9	+ 4.4	Nov	+ 5.2	+ 3.1	Dec	+ 2.6
Euro area	+ 2.2	Dec	+ 2.4	+ 2.2	+ 2.0	+ 4.2	Nov	+ 3.7	+ 2.2	Q3	+ 1.8
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*										
Finland	+ 0.9	Nov	+ 0.5	na	na	+ 4.3	Nov	+ 1.8	+ 3.6	Q3	+ 4.0
Greece	+ 3.6	Dec	+ 3.1	na	na	+ 6.5	Nov	+ 4.0	na		na
Iceland	+ 4.1	Dec	+ 3.9	na	na	+ 3.9	Nov	+ 6.1	+ 7.3	Nov	+ 5.4
Ireland	+ 2.6	Nov	+ 2.9	na	na	+ 3.5	Nov	– 1.6	+ 3.5	Q3	+ 4.7
Luxembourg	+ 2.5	Nov	+ 2.4	na	na	+ 3.0	Oct	+14.6	+ 2.7	Sep	– 0.1
New Zealand	+ 3.4	Q3	+ 2.5	na	na	+ 6.1	Q3	+ 2.5	+ 3.0	Q3	+ 2.2
Norway	+ 1.8	Dec	+ 1.1	na	na	+24.3	Dec	+ 9.7	+ 2.6	Q3	+ 4.3
Portugal	+ 2.6	Nov	+ 2.5	na	na	+ 3.4	Nov	+ 5.2	– 0.1	Oct	– 2.4

*RPI inflation rate 2.4% in Nov. †Aug-Oct.

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Economic forecasts

Jan 12th 2006
From The Economist print edition

The Economist poll of forecasters, January averages (previous month's, if changed)

	Real GDP, % change Low/high range		Real GDP, % change average		Consumer prices % increase		Current account % of GDP	
	2005	2006	2005	2006	2005	2006	2005	2006
Australia	2.4/3.8	2.8/3.9	2.7 (2.6)	3.2 (3.3)	2.8	2.9 (2.8)	-5.9	-5.3
Austria	1.3/2.0	1.8/2.4	1.8 (1.6)	2.0	2.3	1.9 (2.0)	nil	-0.1 (-0.2)
Belgium	1.2/1.5	1.6/2.3	1.4 (1.3)	1.9 (1.8)	2.5	2.1 (2.0)	2.2 (2.3)	2.2 (2.3)
Britain	1.6/1.8	1.7/2.4	1.7	2.1	2.1 (2.2)	2.0 (2.1)	-2.1(-1.7)	-2.2 (-1.9)
Canada	2.8/3.0	2.7/3.6	2.9	3.1 (3.0)	2.3 (2.4)	2.3 (2.4)	1.8 (1.6)	1.6
Denmark	1.9/3.5	2.3/3.3	3.0 (2.4)	2.8 (2.4)	1.8 (2.0)	1.9 (2.0)	2.9	2.8 (2.6)
France	1.4/1.7	1.6/2.2	1.5 (1.6)	1.9	1.9	1.7	-1.2(-1.1)	-1.0 (-0.9)
Germany	0.9/1.2	1.5/2.0	1.1 (1.0)	1.7 (1.5)	2.0	1.7 (1.8)	3.9	3.8 (3.7)
Italy	0.1/0.2	1.0/1.7	0.2 (0.1)	1.3 (1.2)	2.1	2.1 (2.0)	-1.5(-1.4)	-1.4 (-1.5)
Japan	2.4/2.6	1.3/3.1	2.5 (2.4)	2.4 (2.2)	-0.2	0.3	3.5 (3.3)	3.4 (3.3)
Netherlands	0.5/1.0	1.5/2.4	0.8 (0.7)	1.9 (1.8)	1.5	na	4.1 (4.2)	4.2
Spain	3.3/3.4	2.8/3.4	3.4	3.0	3.4 (3.3)	3.1	-6.5(-6.0)	-6.8 (-5.7)
Sweden	2.3/2.7	2.8/3.5	2.6 (2.4)	3.1 (2.8)	0.5 (0.8)	1.5 (1.6)	7.0 (7.1)	6.7 (6.5)
Switzerland	1.1/2.0	1.6/2.7	1.8 (1.3)	2.1 (1.8)	1.2 (1.3)	1.1 (1.3)	13.3(12.5)	12.7 (12.0)
United States	3.5/3.7	2.7/3.8	3.6	3.3	3.4 (3.3)	2.9 (3.1)	-6.5	-6.6 (-6.5)
Euro area	1.2/1.5	1.7/2.3	1.4 (1.3)	1.9 (1.8)	2.2	2.0	nil (0.1)	nil (0.1)

Sources: ABN Amro, Deutsche Bank, Economist Intelligence Unit, Goldman Sachs, HSBC Securities, KBC Bank, J.P. Morgan Chase, Morgan Stanley, Decision Economics, BNP Paribas, Royal Bank of Canada, Citigroup, Scotiabank, UBS

Every month *The Economist* surveys a group of forecasters and calculates the average of their predictions for economic growth, inflation and current-account balances for 15 countries and for the euro area. The table also shows the highest and lowest projections for growth. The previous month's figures, where they are different, are shown in brackets. The panel has raised this year's growth forecast for Japan to 2.4%, up from 2.2% in December. It has also become a bit more optimistic about the euro area, now predicted to grow in 2006 by 1.9% rather than last month's 1.8%. Germany is forecast to expand this year by 1.7%, up from 1.5% in December; and Italy by 1.3%, up from 1.2% last month. The panel has lowered its forecast for American inflation in 2006, with consumer prices now tipped to rise by 2.9% compared with 3.1% a month ago.

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Money and interest rates

Jan 12th 2006
From The Economist print edition

	Money supply* % change on year ago			Interest rates % a year (Jan 11th 2006)					
				3-mth money market		2-year	10-year gov't bonds		corporate
	narrow	broad		latest	year ago	gov't bonds	latest	year ago	bonds
Australia	+ 6.6	+ 8.7	Nov	5.63	5.41	5.18	5.22	5.26	6.23
Britain	+ 5.3	+12.1	Nov	4.56	4.81	4.25	4.09	4.51	5.14
Canada	+ 9.3	+ 8.4	Nov	3.39	2.49	3.82	4.08	4.39	5.12
Denmark	+19.2	+12.2	Nov	2.50	2.25	2.86	3.24	3.71	4.92
Japan	+ 5.5	+ 2.0	Dec	0.03	0.02	0.27	1.45	1.36	1.51
Sweden	+ 2.7	+ 7.2	Nov	1.84	2.00	2.50	3.24	3.70	3.27
Switzerland	+ 4.2	+ 6.4	Nov	1.01	0.74	1.61	2.02	2.19	2.23
United States	- 0.2	+ 7.4	Nov	4.45	2.58	4.44	4.45	4.23	5.41
Euro area†	+10.6	+ 7.6	Nov	2.50	2.15	2.84	3.27	3.56	3.77

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. †Germany for bonds. Benchmarks: US 30-year 4.63%, Japan No. 274 1.45%. Central bank rates: US fed funds 4.25%, ECB refinancing 2.25%, BOJ overnight call 0.001%, BOE repo 4.5%. Sources: Bank of Canada, Commerzbank, Danske Bank, J.P. Morgan Chase, Stockholmsbörsen, UBS, Global Insight, Westpac, Thomson Datastream. Rates cannot be construed as banks' offers.

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The Economist commodity price index

Jan 12th 2006

2000=100

	Jan 3rd	Jan 10th*	% change on one month	% change on one year
Dollar index				
All items	147.1	148.0	+ 3.3	+18.3
Food	132.9	130.6	+ 3.3	+10.6
Industrials				
All	165.6	170.5	+ 3.4	+27.1
Nfa†	139.1	141.2	+ 2.8	+15.9
Metals	180.0	186.5	+ 3.6	+32.3
Sterling index				
All items	128.3	127.1	+ 3.6	+25.8
Euro index				
All items	113.5	113.4	+ 2.1	+28.9
Yen index				
All items	159.3	157.2	– 1.5	+30.4
Gold				
$ per oz	528.70	541.70	+ 3.2	+28.4
West Texas Intermediate				
$ per barrel	63.10	63.32	+ 3.3	+38.3

* Provisional. † Non-food agriculturals.

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Stockmarkets

Jan 12th 2006
From The Economist print edition

Market indices

	Jan 11th	2005-06 high	2005-06 low	% change on one week	% change on record high	% change on Dec 31st 2004 in local currency	% change on Dec 31st 2004 in $ terms
Australia (All Ordinaries)	4,781.1	4,781.1	3,905.5	+ 0.3	nil	+18.0	+13.5
Austria (ATX)	3,800.0	3,815.5	2,415.0	+ 1.0	- 0.4	+56.3	+39.1
Belgium (Bel 20)	3,663.2	3,663.2	2,958.8	+ 0.7	- 0.5	+24.9	+11.2
Britain (FTSE 100)	5,731.5	5,731.8	4,783.6	+ 0.3	-17.3	+19.1	+ 9.2
Canada (Toronto Composite)	11,621.0	11,621.0	9,006.2	+ 1.0	nil	+25.7	+29.7
Denmark (OMXCB)	368.1	374.2	257.8	- 1.6	- 1.6	+42.8	+26.7
France (SBF 250)	3,424.4	3,424.4	2,633.6	+ 1.1	-22.0	+30.0	+15.7
(CAC 40)	4,890.5	4,890.5	3,816.1	+ 1.1	-29.4	+28.0	+13.9
Germany (DAX)*	5,532.9	5,537.1	4,178.1	+ 0.2	-31.4	+30.0	+15.7
Italy (S&P/MIB)	36,548.0	36,548.0	30,645.0	+ 0.6	-27.1	+18.3	+ 5.3
Japan (Nikkei 225)	16,363.6	16,428.2	10,825.4	nil	-58.0	+42.4	+27.7
(Topix)	1,672.4	1,685.2	1,109.2	nil	-42.0	+45.5	+30.5
Netherlands (AEX)	446.3	447.9	347.0	+ 0.3	-36.4	+28.2	+14.1
Spain (Madrid SE)	1,183.8	1,183.8	950.9	+ 0.7	nil	+23.4	+ 9.9
Sweden (Affarsvarlden Gen)	299.2	299.4	218.9	+ 0.8	-25.2	+35.3	+16.3
Switzerland (Swiss Market)	7,752.1	7,752.1	5,669.6	+ 0.4	- 7.8	+36.2	+21.1
United States (DJIA)	11,043.4	11,043.4	10,012.4	+ 1.5	- 5.8	+ 2.4	+ 2.4
(S&P 500)	1,294.2	1,294.2	1,137.5	+ 1.6	-15.3	+ 6.8	+ 6.8
(NASDAQ Comp)	2,331.4	2,331.4	1,904.2	+ 3.0	-53.8	+ 7.2	+ 7.2
Europe (FTSEurofirst 300)†	1,307.6	1,309.5	1,038.6	+ 0.5	-23.3	+25.5	+11.7
Euro area (FTSE Euro 100)†	1,116.8	1,116.8	894.4	+ 0.5	-28.0	+24.0	+10.3
World (MSCI)‡	1,311.6	1,311.6	1,115.0	+ 1.3	- 9.5	+12.2	+12.2
World bond market (Citigroup)††	634.3	662.3	608.7	+ 0.4	- 4.2	- 4.8	- 4.8

*Total return index. †In euro terms. ‡Morgan Stanley Capital International Index includes individual markets listed above plus eight others, in $ terms. ††Citigroup World Government Bond Index, total return, in $ terms.

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Trade, exchange rates and budgets

Jan 12th 2006
From The Economist print edition

	Trade balance*, $bn latest 12 months		Current-account balance $bn latest 12 mths		The Economist poll % of GDP, forecast 2005	2006	Exchange rate trade-weighted† 2000=100 Jan 11th	year ago	Currency units per $ Jan 11th	year ago	per £	per euro	per ¥100	Budget balance % of GDP 2005‡
Australia	− 15.0	Nov	− 43.5	Q3	− 5.9	− 5.3	117.9	112.8	1.33	1.30	2.34	1.60	1.16	+ 1.0
Austria	− 1.8	Oct	− 0.1	Oct	nil	− 0.1	103.7§	104.7	0.83	0.75	1.46	–	0.72	− 2.0
Belgium	+ 16.1	Oct	+ 8.2	Sep	+ 2.2	+ 2.2	104.1§	105.6	0.83	0.75	1.46	–	0.72	nil
Britain	−116.9	Nov	− 40.6	Q3	− 2.1	− 2.2	98.0	99.0	0.57	0.53	–	0.69	0.50	− 3.1
Canada	+ 50.9	Oct	+ 19.6	Q3	+ 1.8	+ 1.6	124.8	119.1	1.16	1.20	2.04	1.40	1.02	+ 1.3
Denmark	+ 9.2	Nov	+ 8.7	Nov	+ 2.9	+ 2.8	106.0	106.8	6.17	5.60	10.9	7.46	5.40	+ 2.8
France	− 31.6	Nov	− 31.4	Oct	− 1.2	− 1.0	106.6§	108.3	0.83	0.75	1.46	–	0.72	− 3.2
Germany	+203.6	Nov	+114.0	Nov	+ 3.9	+ 3.8	104.3§	106.2	0.83	0.75	1.46	–	0.72	− 3.9
Italy	− 11.2	Oct	− 28.3	Oct	− 1.5	− 1.4	76.3§	77.5	0.83	0.75	1.46	–	0.72	− 4.3
Japan	+ 98.2	Oct	+164.3	Oct	+ 3.5	+ 3.4	83.9	90.2	114	102	201	138	–	− 6.5
Netherlands	+ 39.3	Oct	+ 44.3	Q3	+ 4.1	+ 4.2	103.6§	105.1	0.83	0.75	1.46	–	0.72	− 1.6
Spain	− 95.2	Oct	− 80.8	Sep	− 6.5	− 6.8	77.1§	77.9	0.83	0.75	1.46	–	0.72	+ 0.3
Sweden	+ 20.3	Nov	+ 24.2	Q3	+ 7.0	+ 6.7	96.1	100.8	7.73	6.81	13.6	9.35	6.76	+ 1.2
Switzerland	+ 6.6	Nov	+ 49.3	Q3	+13.3	+12.7	106.8	108.0	1.28	1.16	2.25	1.55	1.12	− 1.6
United States	−767.8	Oct	−780.6	Q3	− 6.5	− 6.6	85.8	80.3	–	–	1.76	1.21	0.88	− 3.7
Euro area	+ 41.8	Oct	− 12.0	Oct	nil	nil	116.1	119.5	0.83	0.75	1.46	–	0.72	− 2.9
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*													
Finland	+ 11.6	Oct	+ 7.3	Oct	na	na	81.4§	82.3	0.83	0.75	1.46	–	0.72	+ 2.1
Greece	− 34.3	Oct	− 17.0	Oct	na	na	59.8§	60.4	0.83	0.75	1.46	–	0.72	− 4.5
Iceland	− 1.5	Nov	− 2.2	Q3	na	na	109.9**	96.1	61.3	62.5	108	74.2	53.7	+ 2.0
Ireland	+ 40.5	Oct	− 3.7	Q3	na	na	93.6§	96.2	0.83	0.75	1.46	–	0.72	− 0.9
Luxembourg	− 4.6	Oct	+ 3.5	Q3	na	na	104.1§	105.6	0.83	0.75	1.46	–	0.72	− 2.3
New Zealand	− 4.6	Nov	− 9.1	Q3	na	na	138.0	132.1	1.44	1.41	2.54	1.74	1.26	+ 5.3
Norway	+ 46.0	Nov	+ 43.7	Q3	na	na	108.7	107.2	6.64	6.17	11.7	8.03	5.81	+ 15.3
Portugal	− 23.3	Oct	− 16.6	Oct	na	na	93.7**	93.7	0.83	0.75	1.46	–	0.72	− 6.0

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †Bank of England except §IMF, November average. ‡OECD estimate.
**IMF, September average.

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Metal prices

Jan 12th 2006
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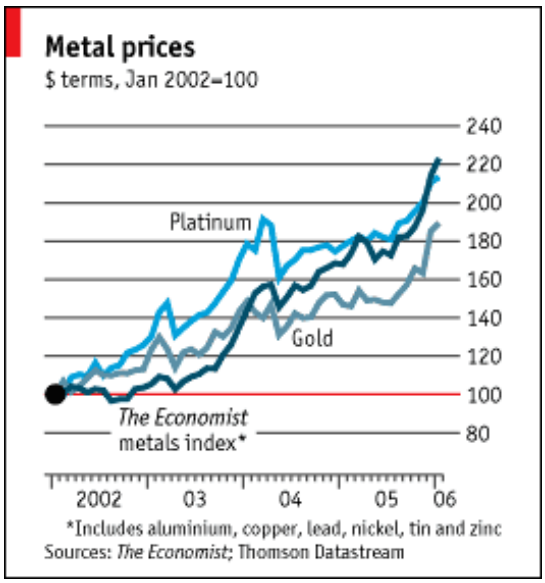
It's a glittering new year for metals. Our metals index rose by 25% in 2005. Copper and zinc prices are at record highs. Aluminium is at a 17-year peak. Gold has reached a 25-year high and platinum is near a 26-year peak.



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Overview

Jan 12th 2006
From The Economist print edition

China's trade surplus more than tripled, to $102 billion in 2005. However, in the 12 months to December, imports rose by 22%, even faster than the 18% rise in exports.

Mexico's inflation rate fell to 3.3% in the year to December, from 5.2% a year earlier. This was its lowest rate over a full year for nearly 40 years. **Argentina's** inflation rate rose to 12.3% over the same period.

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Big Mac index

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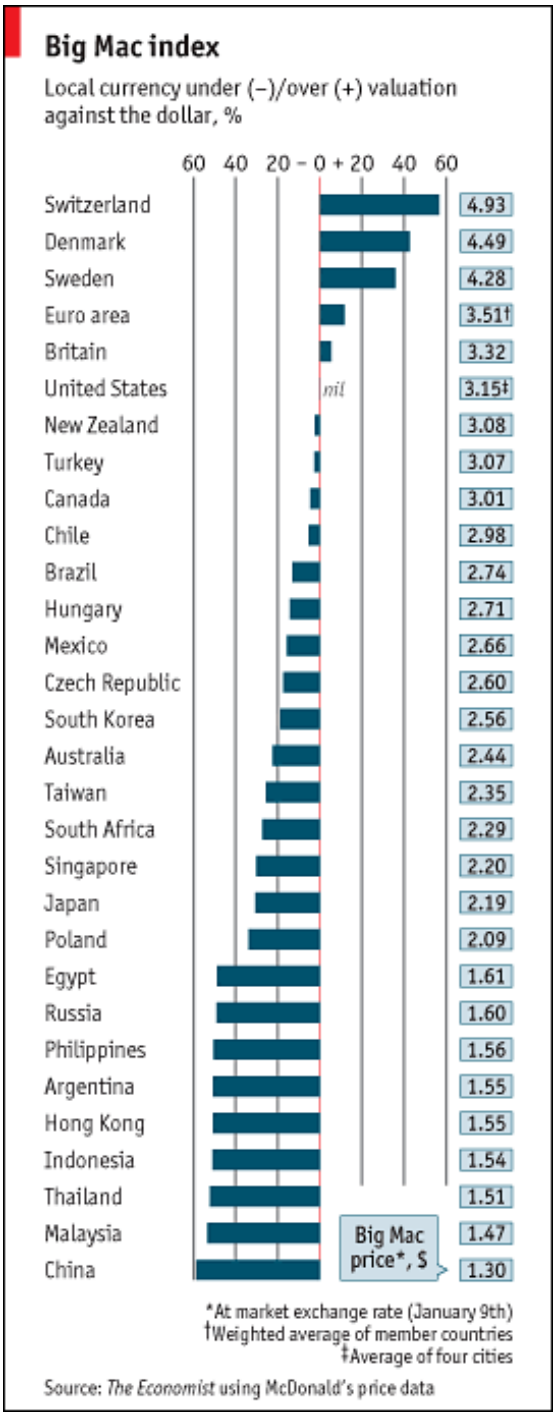
The Economist's Big Mac index is based on the theory of purchasing-power parity, under which exchange rates should adjust to equalise the cost of a basket of goods and services, wherever it is bought around the world. Our basket is the Big Mac. The cheapest burger in our chart is in China, where it costs $1.30, compared with an average American price of $3.15. This implies that the yuan is 59% undervalued.



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MARKETS & DATA

WEEKLY INDICATORS

Economy

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	% change on year ago						Latest 12 months, $bn				Foreign reserves* $bn, latest	
	GDP		Industrial production		Consumer prices		Trade balance		Current account			
China	+ 9.4	Q3	+16.6	Nov	+ 1.3	Nov	+102.1	Dec	+128.5	H1	769.0	Sep
Hong Kong	+ 8.2	Q3	+ 4.1	Q3	+ 1.7	Nov	– 9.4	Nov	+21.0	Q3	124.3	Dec
India	+ 8.0	Q3	+ 6.9	Nov	+ 5.3	Nov	–37.3	Nov	–18.3	Q3	131.0	Dec
Indonesia	+ 5.3	Q3	– 5.9	Oct	+17.1	Dec	+26.2	Nov	+ 0.7	Q3	31.7	Nov
Malaysia	+ 5.3	Q3	+ 6.7	Nov	+ 3.5	Nov	+25.6	Nov	+18.7	Q3	72.5	Nov
Pakistan	+ 8.4	2005†	+11.0	Jun	+ 7.9	Nov	– 8.9	Nov	– 3.7	Q3	9.6	Nov
Philippines	+ 4.1	Q3	+ 4.6	Oct	+ 6.6	Dec	– 2.2	Oct	+ 2.9	Sep	15.8	Dec
Singapore	+ 7.7	Q4	+22.4	Nov	+ 1.0	Nov	+17.3	Nov	+33.7	Q3	116.6	Dec
South Korea	+ 4.5	Q3	+12.2	Nov	+ 2.6	Dec	+23.5	Dec	+18.1	Nov	208.2	Nov
Taiwan	+ 4.4	Q3	+ 9.0	Nov	+ 2.2	Dec	+ 7.8	Dec	+ 8.9	Q3	253.3	Dec
Thailand	+ 5.3	Q3	+ 5.0	Nov	+ 5.8	Dec	– 8.0	Nov	– 3.2	Nov	49.4	Nov
Argentina	+ 9.2	Q3	+ 7.5	Nov	+12.3	Dec	+11.1	Nov	+ 4.4	Q3	25.7	Nov
Brazil	+ 1.0	Q3	+ 0.4	Oct	+ 6.2	Nov	+44.8	Dec	+14.9	Nov	64.3	Nov
Chile	+ 5.2	Q3	+ 6.2	Nov	+ 3.7	Dec	+ 9.2	Dec	– 0.2	Q3	16.0	Nov
Colombia	+ 5.8	Q3	+ 0.5	Oct	+ 4.9	Dec	+ 1.5	Oct	– 1.7	Q3	14.6	Nov
Mexico	+ 3.3	Q3	+ 3.0	Nov	+ 3.3	Dec	– 8.6	Nov	– 8.4	Q3	71.2	Oct
Peru	+ 7.2	Oct	+ 4.1	Oct	+ 1.5	Dec	+ 4.6	Nov	+ 0.8	Q3	13.2	Dec
Venezuela	+ 9.8	Q3	+10.8	Oct	+14.4	Dec	+28.2	Q3	+21.6	Q3	24.4	Oct
Egypt	+ 5.2	Q1	+ 4.0	2005†	+ 3.4	Nov	–11.3	Q3	+ 1.8	Q3	20.0	Nov
Israel	+ 5.7	Q3	–15.2	Oct	+ 2.7	Nov	– 7.9	Dec	+ 2.4	Q3	27.9	Dec
Saudi Arabia	+ 6.2	2005‡	na		+ 1.0	Sep	+84.6	2004	+51.9	2004	27.6	Nov
South Africa	+ 4.9	Q3	+ 0.3	Oct	+ 3.4	Nov	– 3.4	Nov	–10.3	Q3	18.6	Dec
Czech Republic	+ 4.9	Q3	+ 7.2	Nov	+ 2.2	Dec	+ 1.5	Nov	– 3.4	Q3	29.3	Dec
Hungary	+ 4.5	Q3	+ 7.3	Nov	+ 3.3	Nov	– 3.5	Oct	– 8.7	Q3	17.5	Dec
Poland	+ 3.7	Q3	+ 8.5	Nov	+ 1.0	Nov	– 3.0	Oct	– 4.5	Oct	39.9	Nov
Russia	+ 7.0	Q3	+ 5.5	Nov	+10.9	Dec	+117.6	Nov	+81.2	Q3	164.7	Nov
Turkey	+ 7.0	Q3	+10.7	Nov	+ 7.7	Dec	–43.2	Nov	–21.7	Nov	47.9	Nov
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Estonia	+10.8	Q3	+10.4	Nov	+ 3.6	Dec	– 2.5	Oct	– 1.4	Oct	1.8	Nov
Latvia	+11.4	Q3	+ 5.9	Nov	+ 7.0	Dec	– 2.9	Oct	– 1.8	Oct	2.2	Nov
Lithuania	+ 7.6	Q3	na		+ 3.0	Dec	– 3.5	Oct	– 1.6	Oct	3.5	Nov
Slovakia	+ 6.2	Q3	+ 5.7	Nov	+ 3.4	Nov	– 1.9	Nov	– 2.8	Sep	14.9	Nov
Slovenia	+ 3.7	Q3	+ 7.3	Nov	+ 2.3	Dec	– 1.6	Nov	+ 0.1	Oct	8.0	Oct

*Excluding gold, except Singapore; IMF definition. †Year ending June. ‡Economist Intelligence Unit estimate.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Reuters; WM/Reuters; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; Bank Leumi le-Israel; Standard Bank Group

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Financial markets

Jan 12th 2006
From The Economist print edition

	Currency units			Interest rates	Stockmarkets	% change on		
	per $		per £	short-term	Jan 11th		Dec 31st 2004	
	Jan 11th	year ago	Jan 11th	% a year		one week	in local currency	in $ terms
China	8.07	8.28	14.2	2.18	1,272.3	+2.4	- 4.4	- 1.9
Hong Kong	7.75	7.79	13.6	4.08	15,650.9	+3.0	+ 10.0	+ 10.3
India	44.2	43.6	77.8	5.93	9,445.3**	-2.1	+ 43.1	+ 40.7
Indonesia	9,465	9,195	16,664	14.31	1,261.3	+4.1	+ 26.1	+ 23.7
Malaysia	3.75	3.80	6.60	3.25	909.6	+1.4	+ 0.2	+ 1.7
Pakistan	59.8	59.4	105.28	8.76	9,990.2**	+1.4	+ 60.7	+ 59.5
Philippines	52.6	55.9	92.7	6.75	2,150.7	+0.6	+ 18.0	+ 25.8
Singapore	1.63	1.63	2.87	3.28	2,418.7	+1.4	+ 17.1	+ 17.3
South Korea	985	1,043	1,734	4.17	1,394.1	-0.6	+ 55.6	+ 63.6
Taiwan	32.1	31.9	56.5	1.65	6,735.9	+1.8	+ 9.7	+ 8.4
Thailand	39.7	38.9	69.9	4.50	764.0	+2.8	+ 14.4	+ 11.9
Argentina	3.05	2.95	5.37	8.88	1,649.7	+2.4	+ 19.9	+ 16.8
Brazil	2.27	2.69	4.00	17.95	35,952.2	+2.7	+ 37.2	+ 60.2
Chile	524	565	922	5.16	9,457.0	+1.4	+ 5.5	+ 11.9
Colombia	2,275	2,353	4,005	6.23	9,988.4	+4.7	+129.8	+137.7
Mexico	10.6	11.2	18.7	7.92	19,160.4	+2.6	+ 48.3	+ 55.7
Peru	3.44	3.27	6.06	3.60	4,676.8	-4.8	+ 26.0	+ 20.0
Venezuela	2,653§	2,829§	4,670	10.37	21,960.7	+8.5	- 26.7	- 28.7
Egypt	5.74	5.92	10.11	8.57	59,278.1**	+3.5	+141.1	+155.0
Israel	4.63	4.35	8.15	4.91	837.7	-2.2	+ 30.1	+ 21.4
Saudi Arabia	3.75	3.75	6.60	4.98	17,675.9**	+1.0	+115.4	+115.4
South Africa	6.08	5.95	10.7	7.10	18,594.2	+1.0	+ 46.9	+ 36.2
Czech Republic	23.7	22.9	41.8	2.17	1,517.3	+1.4	+ 47.0	+ 38.3
Hungary	207	186	364	6.17	22,429.3	+3.4	+ 52.1	+ 33.1
Poland	3.13	3.06	5.51	4.49	38,091.0	+1.2	+ 43.0	+ 36.8
Russia	28.4	27.8	50.1	12.00	1,216.7‡	+8.1	+103.3	+ 98.1
Turkey	1.34	1.35	2.36	14.81	41,905.4**	+1.3	+ 67.8	+ 69.1
EM (MSCI)*	1.00	1.00	1.76	na	753.2	+2.5	+ 38.9	+ 38.9
EMBI+†	1.00	1.00	1.76	na	371.2	-0.1	+ 12.6	+ 12.6

*Emerging Mkts. †J.P. Morgan Chase's Emerging Mkts Bond Index Plus. ‡In $ terms. §Floating exchange rate. **Latest.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Reuters; WM/Reuters; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; Bank Leumi le-Israel; Standard Bank Group

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Correction: Stockmarkets

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Last week's chart on stockmarkets was in local currency terms, not dollar terms as stated. Sorry. (The online version has been corrected.)

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